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**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**Form 10-K**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended **December 31, 2001**      Commission file number **1-106**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from      to

**LYNCH CORPORATION**

*(Exact name of Registrant as specified in its charter)*

**Indiana**

*(State or other jurisdiction of  
Incorporation or organization)*

**38-1799862**

*(I.R.S. Employer  
Identification No.)*

**50 Kennedy Plaza, Suite 1250,  
Providence, RI**

*(Address of principal executive offices)*

**02903**

*(Zip Code)*

**Registrant's telephone number, including area code:**

**(401) 453-2007**

**Securities registered pursuant to Section 12(b) of the Act:**

**Title of each class**

**Name of each exchange on which registered**

Common Stock, No Par Value

American Stock Exchange

**Securities registered pursuant to section 12(g) of the Act: None**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.    Yes       No

Indicate by mark if disclosure of delinquent filers pursuant to Item 405 of Regulations S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K.   

The aggregate market value of voting stock held by non-affiliates of the Registrant (based upon the closing price of the Registrant's Common Stock on the American Stock Exchange on March 15, 2002 of \$17.00 per share) was \$17,719,729. (In determining this figure, the Registrant has assumed that all of the Registrant's directors and officers are affiliates. This assumption shall not be deemed conclusive for any other purpose.)

The number of outstanding shares of the Registrant's Common Stock was 1,497,883 as of March 15, 2002.

**DOCUMENTS INCORPORATED BY REFERENCE:**

Part III: Certain portions of Registrant's Proxy Statement for the 2002 Annual Meeting of Shareholders.

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## FORWARD LOOKING INFORMATION

This document contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this discussion and throughout this document, words, such as “intends,” “plans,” “estimates,” “believes,” “anticipates” and “expects” or similar expressions are intended to identify forward-looking statements. These statements are based on the Registrant’s current plans and expectations and involve risks and uncertainties, over which the Registrant has no control, that could cause actual future activities and results of operations to be materially different from those set forth in the forward-looking statements. Important factors that could cause actual future activities and operating results to differ include fluctuating demand for capital goods such as large glass presses, delay in the recovery of demand for components used by telecommunications infrastructure manufacturers, and exposure to foreign economies. Important information regarding risks and uncertainties is also set forth elsewhere in this document, including in Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations”. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Registrant undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. All subsequent written or oral forward-looking statements attributable to the Registrant or persons acting on its behalf are expressly qualified in their entirety by these cautionary statements. Readers are also urged to carefully review and consider the various disclosures made by the Registrant, in this document, as well as the Registrant’s periodic reports on Forms 10-K, 10-Q and 8-K, filed with the Securities and Exchange Commission (“SEC”).

### PART I

#### Item 1. *Business*

The Registrant, Lynch Corporation (hereinafter referred to as “Registrant,” “Company” or “Lynch”), incorporated in 1928 under the laws of the State of Indiana, is a diversified holding company with subsidiaries engaged in manufacturing. Lynch’s executive offices are located at 50 Kennedy Plaza, Suite 1250, Providence, RI 02903. Its telephone number is (401) 453-2007.

Lynch has two wholly-owned subsidiaries, M-tron Industries, Inc., a Delaware corporation (“M-tron”), and Lynch Systems, Inc., a South Dakota corporation (“LS” or “Lynch Systems”). Registrant also owns 41.8% of the equity (and 49.5% of the voting power) of Spinnaker Industries, Inc., a Delaware corporation (“Spinnaker”).

Registrant’s business development strategy is to expand its existing operations through internal growth and acquisitions. It may also, from time to time, consider the acquisition of other assets or businesses that are not related to its present businesses. As used herein, the Registrant includes subsidiary corporations.

On September 1, 1999, Registrant spun off to its shareholders the stock of Lynch Interactive Corporation, which holds the multimedia and service operations previously owned by Registrant and which accounted for approximately 40% of the Registrant’s 1998 revenues and 47.6% of Registrant’s total assets at December 31, 1998.

#### A. **Lynch Systems, Inc.**

##### *Overview*

Lynch Systems, Inc. (“LS” or “Lynch Systems”), a 100% owned subsidiary of Registrant, designs, develops, manufactures and markets a broad range of manufacturing equipment for the electronic display and consumer glass industries. LS also produces replacement parts for various types of packaging and glass container-making machines, which LS does not manufacture.

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### ***Selected Financial Information***

For financial reporting purposes, Lynch Systems comprises the Registrant's "glass manufacturing equipment" segment. For information about this segment's net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included herein.

### ***Lynch Systems Objectives***

LS intends to continue to build on its name recognition and reputation as one of the world's leading manufacturers of glass forming machinery. LS is the only independent supplier in the CRT (cathode ray tube) glass forming field and it is LS's intention to use this strength to form closer partnerships with its customers in their pursuit of innovative glass making machinery.

LS's long term intentions are to monitor the market direction and to be at the forefront of technology in order to respond to market demand for new and innovative types of machinery needed to produce glass. LS intends to continue to research and develop state-of-the-art machinery within its core competence, and also to seek new markets where its experience and proven success can be utilized to develop new products and increase its growth.

LS also intends to continue to expand on its new expertise obtained from Lynch AMAV in the feeder and shear markets (discussed below) and to reduce the cost of its raw materials by continuing to search for cheaper suppliers of materials, especially from foreign markets. In addition, LS intends to continue its own in-house cost cutting programs by eliminating redundant or superfluous operations, improving its factory quality and yield rates and better utilization of its current personnel. By increasing its efficiency and shortening its delivery rate, LS hopes to increase the number of turns giving a positive effect to its financial performance. There is no assurance that LS can attain these objectives.

### ***Products and Manufacturing***

LS manufactures glass-forming presses and electronic controls to provide high-speed automated systems to form different sizes of face panels and CRT display tubes for television screens and computer monitors including presses to build large screen televisions for the HDTV (high definition television) market. LS also manufactures and installs forming equipment that sizes, cuts, and forms tableware such as glass tumblers, plates, cups, saucers and commercial optical glass. Additionally, LS manufactures and installs fire polishing, electronic controls and retrofit systems for CRT display and consumer glass presses.

At year-end 1998, LS, through a subsidiary, entered into a joint venture, Lynch-AMAV LLC, with AMAV GmbH of Germany to develop and manufacture glass-manufacturing equipment for the tableware industry. LS has a 75% interest in the joint venture. The joint venture designs and develops feeders, shears and presses, most of which are manufactured for the joint venture by LS. LS believes that this joint venture has expanded LS's glass tableware equipment business, particularly in Europe.

The production of glassware entails the use of machines, which heat glass and, using great pressure, form an item by pressing it into a desired shape. Because of the high cost of bringing the machine and materials up to temperature, a machine for producing glassware must be capable of running 24 hours a day, 365 days a year.

During 2001, LS, including Lynch-AMAV, built TV (television) and consumer glass press machines for customers, as well as selling feeders, shears and spare parts. LS delivered four large TV glass press machines in 2001. These four large machines had a selling price of approximately \$14 million, all of which was recognized as income in 2001. In 2001 LS sold four additional large TV glass press machines to be delivered in 2002. These additional machines sold for approximately \$14 million, of which \$5.5 million was recognized as income in 2001 using the percentage of completion method and the balance of \$8.5 million will be recognized in 2002.

At December 31, 2001, LS had orders for \$12 million for large TV glass press machines as well as for glass press machines, feeders, shears and spare parts for the tableware market, all of which are scheduled to be

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delivered in 2002. LS is also in negotiations to obtain other orders for large TV glass presses; however, there can be no assurance that LS will obtain any other orders.

LS's worldwide customers require capital equipment that produces a wide variety of Tableware products to remain competitive. In support of this market demand, Lynch Systems has invested in R&D programs to manufacture new lines of capital equipment such as Stretch Machines for one-piece Stemware, Firepolishers for high quality Tableware and Spinning Machines for high speed, high quality Dishware.

To further expand LS's Tableware product lines, additional product lines have been acquired through royalty partnerships with leading Industry concerns. In 1999, LS acquired the H-28 Press and Blow machine from Emhart. This high production machine produces both round and geometric design Tumblers and is now marketed by LS as the LH-28 with numerous Electronic Control improvements. In 2000, the Eldred product line of Burnoff Machines, used to fire finish the rims of the H-28 Tumblers, and four-color Decorating Machines were acquired by LS. All Tableware capital equipment requires moulds in the production of any article. In 2002, agreement was reached with Merkad, a producer of high quality moulds, to represent and distribute moulds throughout North and South America.

LS has the capabilities to take a glass product idea from a customer, have our engineering staff design a machine that will mass produce this glass product and then build the final machine for the customer.

### ***International Sales***

LS's revenues from international sales were \$22.9 million, \$20.3 million and \$4.7 million for 2001, 2000 and 1999, respectively, representing approximately 88%, 88% and 83% of LS's net sales for 2001, 2000 and 1999, respectively. The profitability of international sales is approximately equivalent to that of domestic sales. Because many international orders require partial advance deposits, with the balance often secured by irrevocable letters of credit from banks in the foreign country, the Registrant believes that some of the credit risks commonly associated with doing business in international markets are minimized. The Registrant avoids currency exchange risk by transacting substantially all international sales in United States dollars.

### ***Backlog***

LS had an order backlog of approximately \$12 million at December 31, 2001, compared with approximately \$13.5 million at December 31, 2000. All of LS's \$12 million backlog as of December 31, 2001 is scheduled to be delivered in 2002. LS includes as backlog only those orders which are subject to written contract or written purchase orders. In 1998, LS received \$2.4 million in connection with the cancellation of a \$16 million dollar order for large TV glass presses and parts, which amount can be used by the customer as a credit for future orders. The \$2.4 million has been reduced to \$1.5 million as of December 31, 2001 as a result of sales to this customer.

### ***Competition***

LS believes that in the worldwide pressware market it is the largest supplier to glass companies that do not manufacture their own pressware machines. Competitors include various companies in Italy, Japan, Korea, Germany and elsewhere. While several of the largest domestic and international producers of glass pressware frequently build their own glass-forming machines and produce spare parts in-house, nearly all pressware producers have made purchases of machines and/or spare parts from LS.

### ***Customers***

LS's business is not dependent upon a single customer or a few customers.

### ***Raw Materials***

Raw materials are generally available to LS in adequate supply from a number of suppliers.

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### ***Research and Development***

Research and development expense was \$146,000 in 2001 and zero in each of 2000 and 1999. R&D expense for 2002 is budgeted at \$100,000.

### ***Intellectual Property***

Lynch Systems owns patents and proprietary know-how which are important to its business and the maintenance of its competitive position. Its most important patent is for a rotary glass-molding press with cushioned trunnion mounted hydraulic drive, expiring October, 2012. Lynch System's investment in Lynch-AMAV, discussed above, has given Lynch Systems access to important proprietary know-how and technology which has enabled Lynch Systems to expand its product offerings and customer base.

### ***Employees***

Lynch Systems employs approximately 93 employees at its Bainbridge, Georgia facility and 7 employees at Lynch-AMAV in Germany, none of whom belong to a union.

## **B. M-tron Industries, Inc. ("M-tron")**

### ***Overview***

M-tron, a wholly-owned subsidiary of Lynch, is a designer, manufacturer and marketer of custom designed electronic components that are used primarily to control the frequency or timing of electronic signals in communications equipment. Its devices, which are commonly called frequency control devices, crystals or oscillators, support fixed and mobile wireless, copper wire, coaxial cable, wide area networks, local area networks and fiber optic systems. It sells its products to original equipment manufacturers, contract manufacturers and to distributors.

M-tron's products are quartz crystal based frequency control devices consisting of packaged quartz crystals and oscillators incorporating those crystals. Its products enable communications equipment manufacturers and network equipment manufacturers to meet the increasing demands of their customers because they produce an electrical signal that is:

- accurate — the frequency of the signal does not change significantly over a period of time;
- stable — the frequency of the signal does not vary significantly when our product is subjected to a range of operating temperatures; and
- has low electronic noise — the signal does not add interfering signals that can degrade the performance of the electronics system.

In addition, M-tron sells crystals and oscillators which are used outside the communications industry. These frequency control devices are used in microprocessor and computer applications, industrial controls, medical instrumentation, automotive products and military applications.

M-tron has over 35 years of experience designing, manufacturing and marketing crystal based frequency control products. Its customers rely on the skills of M-tron's engineering and design team to help them solve frequency control problems during all phases of their product's life cycles, including product design, prototyping, manufacturing and subsequent product improvements.

### ***Selected Financial Information***

For financial reporting purposes, M-tron comprises the Registrant's "frequency control devices" segment. For information about this segment's net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included herein.



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### ***M-tron Objectives***

M-tron's objective is to build on the strength of its core expertise in packaged quartz crystal and oscillator technologies to become the supplier of choice to original equipment manufacturers who supply infrastructure equipment to the communications and networking industries.

M-tron intends to maintain its current investment in technical resources, including design and engineering personnel to enable it to provide a high level of design and engineering support to its customers. It believes that technical participation with its original equipment manufacturers customers in the early stages of their design process will lead to M-tron's frequency control devices being designed into their products more regularly.

M-tron intends to increase the use of its offshore contract manufacturers who have added capacity on its behalf. However, during the current economic slowdown, this additional capacity is not being fully utilized. In addition, M-tron's long term objective is to reduce the time it takes to manufacture its products which will result in further increases in its manufacturing capacity. To that end, it has dedicated additional resources to evaluating its manufacturing processes and to identifying and implementing process improvements.

M-tron believes that it can significantly enhance its business opportunities by acquiring technology, product portfolios and/or customer bases. Some of these may offer immediate sales opportunities while others may meet longer term objectives. It plans to pursue these opportunities by making strategic acquisitions or by acquiring or licensing technology.

M-tron intends to design, manufacture and sell devices that offer higher frequencies or greater precision than its current products. These devices will serve applications within the communications and networking industries for which it does not currently provide products. It intends to achieve this through a combination of focused research and development and strategic acquisitions, if they are appropriate.

There is no assurance that M-tron can achieve these objectives.

### ***Products***

M-tron's products are high quality, reliable, technically advanced frequency control devices, including packaged quartz crystals and oscillators incorporating those crystals.

M-tron designs and produces a range of packaged quartz crystals and quartz crystal based oscillators. There are a variety of features in its product family. The Packaged Crystal is a single crystal in a hermetically sealed package and is used by electronic equipment manufacturers, along with their own electronic circuitry, to build oscillators for frequency control in their electronic devices. The Clock Oscillator is the simplest of its oscillators. It is a self-contained package with a crystal and electronic circuitry that is used as a subsystem by electronic equipment manufacturers to provide frequency control for their devices. The Voltage Controlled Crystal Oscillator (VCXO) is a variable frequency oscillator whose frequency can be changed by varying the control voltage to the oscillator. The Temperature Compensated Crystal Oscillator (TCXO) is an oscillator designed for use over a range of temperatures. The Digitally Compensated Crystal Oscillator (DCXO) is a temperature compensated oscillator in which the compensation electronics are digital and offer greater frequency stability than the TCXO over a range of temperatures. This variety of features in M-tron's product family offers the designers at electronic equipment manufacturers a range of options as they create the needed performance in their products.

Currently, M-tron's oscillator products operate at frequencies ranging from 32 kilohertz to over 800 megahertz which constitute most of the oscillator frequencies that are now used in communications equipment. However, many of its products, through amplification or other means, are ultimately incorporated into those products that operate at frequencies in excess of 800 megahertz.

M-tron's products are employed in numerous applications within the communications industry, including computer and telephone network switches, high-speed gigabit Ethernet, modems, wireless transmitters/receivers, multiplexers, data recovery/regeneration devices, fiber channel networks, repeaters, data

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transceivers, line interface devices and base station controllers. Its products are incorporated into end products that serve all elements of the communications industry.

The crystals and oscillators M-tron sells for use in non-communications applications are used in industrial applications such as security systems, metering systems, electronic test instruments and industrial control systems. They are used in military and medical instrumentation applications as well as in various computer peripheral equipment such as printers, modems, monitors, video cards and sound cards. These non-communications applications may not require the quality and reliability demanded by manufacturers of communications equipment.

### ***Research and Development***

At December 31, 2001, M-tron employed 10 engineers and technicians in South Dakota who devoted most of their time to research and development. M-tron intends to maintain the number of engineers and technicians who perform research and development in 2002. Its research and development expense was approximately \$1,348,000 in 2001, \$994,000 in 2000 and \$856,000 in 1999. At its current level of resources, which is reduced from the level of 2001, M-tron expects to reduce its spending on research and development by 25% during 2002.

### ***Customers***

M-tron markets and sells its frequency control devices primarily to:

- original equipment manufacturers of communications and networking equipment;
- contract manufacturers for original equipment manufacturers; and
- distributors who sell to original equipment manufacturers and contract manufacturers.

In 2001, Celestica (with Primetech) accounted for approximately 14% of M-tron's net sales, compared to less than 10% in 2000. No other customer accounted for more than 10% of its 2001 revenues. Sales to its ten largest customers accounted for approximately 60% of net sales for 2001, 2000 and 1999.

### ***International Sales***

M-tron's revenues from international sales were \$9.5 million, \$17.6 million and \$11.3 million for 2001, 2000 and 1999, respectively, representing approximately 44%, 48% and 43% of its net sales for 2001, 2000 and 1999, respectively. In 2001, this consisted of approximately 27% from customers in Canada, 11% from customers in Asia, 4% from customers in Western Europe and 2% from customers in Mexico. M-tron is increasing its international sales efforts by adding distributors and manufacturers' representatives in Western Europe and Asia.

### ***Backlog***

M-tron had backlog orders of approximately \$1.4 million at December 31, 2001 compared with approximately \$12.4 million at December 31, 2000. However, monthly new orders for the first two months of 2002 were 20% higher than the average monthly orders for the last three months of 2001. M-tron includes as backlog those orders which are subject to specific production release orders under written contracts, verbal and written orders from distributors with which it has had long-standing relationships, as well as written purchase orders from sales representatives. Its customers may cancel or defer orders without significant penalty.

### ***Competition***

Frequency control devices are sold in a highly competitive industry. There are numerous domestic and international manufacturers who are capable of providing custom designed quartz crystals and oscillator modules comparable in quality and performance to its products. Competitors include Vectron International (a division of Dover Corporation), CTS Corporation and Saronix. M-tron does not operate in the same markets as high volume manufacturers of standard products; rather it focuses on manufacturing lower volumes of

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custom designed frequency control devices. Many of its competitors and potential competitors have substantially greater financial, engineering, manufacturing and marketing resources than it does. M-tron seeks to manufacture custom designed, high performance crystals and oscillators, which it believes it can sell competitively based upon performance, quality, order response time and a high level of engineering support.

### ***Manufacturing***

M-tron has one manufacturing facility in Yankton, South Dakota, and has long-term relationships with two contract manufacturers in Asia. M-tron maintains a rigorous quality control system and is an ISO 9001 qualified manufacturer.

In 1990, M-tron established a working relationship with a contract manufacturer located in South Korea, and in 1994, it established a working relationship with a contract manufacturer located in the People's Republic of China. While it does not have written long term agreements with them, it believes that it is the largest customer for each of these contract suppliers and, as such, believes that from time to time it received preferential treatment on production scheduling matters.

M-tron attempts to utilize standard parts and components that are available from multiple vendors located in the United States or internationally; however, some components used in its products are available from only a limited number of sources.

### ***Intellectual Property***

M-tron has no patents, trademarks or licenses which are considered to be important to M-tron's business or operations. Rather, M-tron believes that its technological position depends primarily on the technical competence and creative ability of its engineering and technical staff in areas of product design and manufacturing processes as well as proprietary know-how and information.

### ***Employees***

As of December 31, 2001, M-tron employed 136 people. It has also employed independent contractors and temporary employees. None of its employees is represented by a labor union and it considers its employee relations to be good.

## **C. Spinnaker Industries, Inc. ("Spinnaker")**

Lynch (through its subsidiary LS) currently owns 1,829,063 shares of the Class A Common Stock and 1,237,203 shares of the Common Stock of Spinnaker Industries, Inc. ("Spinnaker"). Lynch's combined holdings in Spinnaker represent 41.8% and 49.5% of the equity and voting power of Spinnaker, respectively. Spinnaker conducts its business through two wholly-owned subsidiaries, Spinnaker Coating, Inc. ("Spinnaker Coating") and Entoleter, Inc. ("Entoleter").

### ***Deconsolidation***

Prior to September 30, 2001, Lynch owned 48% and 60%, respectively, of the equity and voting power of Spinnaker. As such, under accounting principles generally accepted in the United States, Lynch consolidated the results of Spinnaker and was required to record all of the losses of Spinnaker, since the non-Lynch interests were not required to absorb their shares of losses (52%) after their investment was fully absorbed by losses. On September 26, 2001, Lynch caused LS to make a charitable disposition of 430,000 shares of Spinnaker's Class A Common Stock. As a result of that transaction: (a) Lynch's equity interest and voting power in Spinnaker were reduced to their current level of 41.8% and 49.5%, respectively, (b) Lynch deconsolidated Spinnaker for financial reporting purposes, effective September 30, 2001, (c) since September 30, 2001, Lynch has accounted for its ownership of Spinnaker using the equity method of accounting and (d) Lynch will not record any additional losses from Spinnaker, as Lynch has no obligation to further fund such losses.

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### ***Spinnaker Chapter 11 Reorganization Proceeding***

On November 13, 2001 (the “Filing Date”), Spinnaker and its Spinnaker Coating, Spinnaker Coating-Maine, Inc. and Entoleter subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code (11 U.S.C. §101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the “Court”). The cases are being jointly administered under Case No. 01-38066.

Effective December 28, 2001, Spinnaker’s Common Stock and Class A Common Stock were de-listed from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligation to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the “Letter of Intent”) with WR Capital Partners, LLC (“WR Capital”) whereby SP Acquisition LLC (“SP Acquisition”), an acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker’s (and its subsidiaries’) assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations). Entoleter’s assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement (as amended, the “Asset Purchase Agreement”) with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker’s assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker’s equity holders.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter’s assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 5, 2002. If the sale closes, Spinnaker estimates that pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter’s sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (i) and (ii), liquidate Entoleter’s assets.

Spinnaker’s business and properties are described below (in this Section C of Item 1 and in Item 2) without regard to the impact of Spinnaker’s reorganization proceeding and the sale of its assets pursuant thereto.

#### ***Business***

Spinnaker, through Spinnaker Coating, is a manufacturer and marketer of adhesive-backed material, primarily for the pressure sensitive label stock market.

Spinnaker Coating primarily manufactures custom, low-volume, pressure sensitive products used for specialty applications. Customers convert its label stock into labels used for a broad range of end use applications, including bar-coding, mailing and shipping, packaging for pharmaceutical, food and other consumer products, office identification and business forms, postage stamps, decorative labels and other specialty industrial uses. Spinnaker Coating is the largest supplier of pressure sensitive postage stamp stock for ultimate use by the United States Postal Service. In March 1998, Spinnaker Coating was selected by Paper Corporation of the U.S. (“PCUS”) to be its exclusive source of pressure sensitive postage stamp stock for delivery under a five year supply contract it was awarded by the U.S. Bureau of Engraving and Printing. Spinnaker also supplies, through PCUS, pressure sensitive postage stamp stock to private printers who supply postage stamps directly to the United States Postal Service.

In March 1998, Spinnaker Coating acquired the pressure sensitive manufacturing facilities of S.D. Warren Company (“Warren”) in Westbrook, Maine for an aggregate purchase price of approximately

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\$51.8 million plus the assumption of certain liabilities (excluding substantially all trade payables). The purchase price was paid by the issuance of a subordinated convertible note to Warren, in the original principal amount of \$7.0 million, and the remainder with funds available under Spinnaker's asset-backed working capital revolving credit. The facility became unprofitable and was closed in July 2001.

Spinnaker also manufactures and markets industrial process equipment and air pollution control scrubbers through Entoleter.

### ***Selected Financial Information***

For financial reporting purposes, until September 30, 2001 when Spinnaker was deconsolidated from Registrant, Spinnaker Coating comprised the Registrant's "adhesive-backed label stock" segment and Entoleter comprised the "industrial process equipment" segment. For information about these segments' net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included in this report.

### ***Adhesive-backed Label Stock***

Spinnaker Coating develops, manufactures and markets pressure sensitive adhesive-backed label stock that is converted by printers and industrial users into products that are utilized for marking, identifying, labeling and decorating applications and products. To better concentrate on Spinnaker Coating's strengths and market niche, a decision was made by Spinnaker's management to reorganize and realign the business in the fourth quarter of 2000 and going forward in 2001. The restructuring involved the elimination of non-pressure sensitive product lines, outsourcing of non-core manufacturing processes and termination of approximately 100 employees.

Pressure sensitive products, which are activated by the application of pressure, are manufactured with a three-element construction consisting of face stock, adhesive coating and silicone coated release liner. The adhesive product is sold in roll or sheet form for further conversion into products used primarily for marking, identification and promotional labeling. Spinnaker Coating's pressure sensitive products are sold under the trade names Strip Tac® and Strip Tac Plus®. Roll pressure sensitive products are generally sold to label printers that produce products used primarily for informational labels (shipping labels, price labels, warning labels, etc.), product identification and postage stamps. Sheet pressure sensitive products are sold to commercial sheet printers, who provide information labels and other products (such as laser printer stock).

### ***Marketing and Customers***

Spinnaker Coating markets its broad range of products to a variety of customers. Its marketing strategy focuses not only on products but also customer service and specific customer applications. Spinnaker has conducted business with its top 10 customers for approximately 20 years on average. During 2001, one customer, Paper Corporation of the United States, accounted for approximately 17.1% of Spinnaker's net sales.

Spinnaker Coating generally markets its products through its own sales representatives to regional and national printers, converters and merchants. A major portion of sales represent product manufactured and shipped to customers directly from Spinnaker Coating's facilities in Troy, Ohio. However, to broaden its market penetration, Spinnaker Coating also contracts with regional processors throughout the United States, with whom Spinnaker Coating stores product until sold. Generally, these processors perform both slitting and distribution services for Spinnaker Coating.

### ***Manufacturing and Raw Materials***

Spinnaker Coating manufactures its adhesive-backed label stock products at two plants in Troy, Ohio. Spinnaker has made approximately \$8.4 million in capital expenditures at the Ohio facilities over the last five years.

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Raw materials are the most significant cost component in Spinnaker Coating's production process. The material component accounts for approximately 65-75% of the total cost of its products, with the most important raw materials being paper (gumming kraft and face stock), adhesive materials, and polypropylene film. These materials are currently readily available and are procured from numerous suppliers. The cost of Spinnaker's principal raw materials have generally remained stable or decreased over recent years. Historically, the increases in raw material costs for Spinnaker's products have not materially impacted Spinnaker's gross margin. The future impact of a change in raw material costs on Spinnaker's profitability is based, in part, on pricing by Spinnaker's competitors. Although, changes in Spinnaker's raw material costs have recently not materially impacted Spinnaker's gross margin, Spinnaker cannot be assured that future raw material cost increases can be passed through to its customers or that such cost increases will not negatively impact Spinnaker's gross margin.

### ***Competition***

The adhesive-backed label stock industry is highly competitive. Spinnaker Coating competes with several national manufacturers, including the Fasson unit of Avery Dennison and the MACtac unit of Bemis Company, Inc., as well as a number of importers and smaller regional manufacturers. As a result of the competitive environment in the markets in which Spinnaker Coating operates, the company faces (and will continue to face) pricing pressure on its products. As a result of such pricing pressure, Spinnaker Coating has experienced, and may continue to experience, reductions in the profit margins on its sales, or has and may be unable to pass future raw material price increases to its customers (which would also reduce profit margins).

### ***Backlog***

Spinnaker Coating's label stock backlog believed to be firm was \$5.0 million at December 31, 2001, as compared to \$8.4 million at December 31, 2000.

### ***Industrial Process Equipment Business***

Through Entoleter, Spinnaker engineers, manufactures and markets a line of industrial process equipment and a line of air pollution control equipment. Entoleter's net sales consist entirely of sales to commercial and industrial customers.

### ***Environmental Regulations***

Spinnaker's operations are subject to environmental laws and regulations governing emissions to the air, discharges to waterways, and generation, handling, storage, transportation, treatment and disposal of waste materials. Spinnaker is also subject to other federal and state laws and regulations regarding health and safety matters. Environmental laws and regulations are constantly evolving and it is impossible to predict the effect that these laws and regulations will have on Spinnaker in the future. While Spinnaker believes it is currently in substantial compliance with all such environmental laws and regulations, there can be no assurance that it will at all times be in complete compliance with all such requirements. Spinnaker has made, and expects to continue to make, capital expenditures to comply with environmental requirements. As is the case with manufacturers in general, if a release of hazardous substances occurs on or from Spinnaker's properties or any associated offsite disposal location, or if contamination from prior activities is discovered at any of Spinnaker's properties, Spinnaker may be held liable and the amount of such liability could be material.

### ***Patents and Trademarks***

Patents are held by Spinnaker with respect to the manufacture of certain of its products, but its management does not consider such patents to be important to Spinnaker's operations. The patents expire over various lengths of time with the last patent expiring in about 10 years. Spinnaker has registered several of its trade names and trademarks for adhesive-backed materials.

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### ***International Sales***

Spinnaker's international sales were \$13.3 million, \$20.1 million and \$17.5 million in 2001, 2000 and 1999, respectively, representing approximately 11.4%, 17.4%, and 10.8% of Spinnaker's net sales for 2001, 2000 and 1999, respectively. Of the \$13.3 million in 2001 international sales, approximately 99% were represented by exports of Spinnaker Coating. The substantial majority of these sales were to Canadian customers and, consequently, Spinnaker believes that the risks commonly associated with doing business in international countries are minimal. The gross margin on international sales is substantially equivalent to that of domestic sales. Because international sales are transacted in United States dollars, payments in many cases are secured by irrevocable letters of credit.

### ***Employees***

As of December 31, 2001, Spinnaker employed 263 persons, of whom 231 were Spinnaker Coating employees and 32 were Entoleter employees. Spinnaker Coating's Troy, Ohio plants began negotiating a collective bargaining agreement with the Paper, Allied Industrial, Chemical and Energy Workers International Union, AFL-CIO ("PACE") in February 2001, but have yet to reach an agreement. This agreement will cover approximately 132 hourly employees. Entoleter's approximately 14 hourly production employees are members of the United Electrical, Radio and Machine Workers of America Union. The current collective bargaining agreement expires in 2002. Spinnaker and Entoleter believe that their relations with their employees are good; however, there can be no assurance that they will not experience work stoppages or slowdowns in the future.

## **D. Other Information**

While the Registrant holds licenses and patents of various types, Registrant does not believe they are critical to its overall operations. See respective "Intellectual Property" sections for each of Lynch Systems, M-tron and Spinnaker above.

The Registrant conducts product development activities with respect to each of its major lines of business. Currently, such activities are directed principally toward the improvement of existing products, the development of new products and/or diversification. In the last three years, M-tron has accounted for the vast majority of Registrant's product development costs.

The capital expenditures, earnings and competitive position of Registrant have not been materially affected to date by compliance with current federal, state, and local laws and regulations relating to the protection of the environment; however, Registrant cannot predict the effect of future laws and regulations. The Registrant has not experienced difficulties relative to fuel or energy shortages. See also "Environmental Regulations" under Item 1. Business — C. Spinnaker Industries, Inc. for more information with respect to Spinnaker.

No portion of the business of the Registrant is regarded as seasonal.

There were no customers in 2001 or 2000 that represent 10% or more of consolidated revenues. The Registrant does not believe that it is dependent on any single customer.

Additional information with respect to each of the Registrant's lines of business is included in Note 15 to the Consolidated Financial Statements included as Item 14(a) below.

## **E. Executive Officers of the Registrant**

Pursuant to General Instruction G (3) of Form 10-K, the following list of executive officers of the Registrant is included in Part I of this Annual Report on Form 10-K in lieu of being included in the Proxy Statement for the 2002 Annual Meeting of Shareholders. Such list sets forth the names and ages of all executive officers of Registrant indicating all positions and offices with the Registrant held by each such person and each such person's principal occupations or employment during the past five years.

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Name	Offices and Positions Held	Age
Ralph R. Papitto	Chairman and Chief Executive Officer (since August 2001) of Lynch; Chief Executive Officer of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2000); Chairman and Chief Executive Officer of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1990-1999); Founder, Chairman and Chief Executive Officer of Nortek, Inc., a NYSE listed manufacturer of construction products (1967-1990); Director of Lynch Interactive Corporation (since 1999); Spinnaker Industries, Inc.; AFC Cable Systems, Inc.; and Global Sports & Gaming.Com; Chairman of the Board of Trustees of Roger Williams University.	75
Mario J. Gabelli	Chairman (1986 to August 2001) and Chief Executive Officer (1986 to January 2000; and April 2001 to August 2001) and Vice Chairman (since August 2001) of Lynch; Chairman, Chief Executive Officer and a Director of Lynch Interactive Corporation (since September 1999); Chairman and Chief Executive Officer of Gabelli Group Capital Partners (since 1980), a private Corporation which makes investments for its own account; Chairman and Chief Executive Officer of Gabelli Asset Management Inc. (since 1999), a NYSE listed holding corporation for subsidiaries engaged in various aspects of the securities business; Director/ Trustee and/or President of all registered investment companies managed by Gabelli Funds, LLC (since 1986); Governor of the American Stock Exchange; Overseer of Columbia University Graduate School of Business; Trustee of Fairfield University, Roger Williams University, Winston Churchill Foundation and E.L. Wigend Foundation; Director of The National Italian American Foundation and The American-Italian Cancer Foundation, Chairman, Patron’s Committee of Immaculate Conception School; and former trustee of Fordham Preparatory School.	59
Richard E. McGrail	President and Chief Operating Officer (since October 2001) of Lynch; President of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2001); Division President of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1993 to 2001); Prior general and marketing management experience with Digital Equipment Corporation (DEC).	47
Raymond H. Keller	Chief Financial Officer, Vice President and Secretary (since October 2001) of Lynch; Chief Financial Officer of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2000); Director and Chief Financial Officer of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1989 to 2000); Trustee of Roger Williams University; Prior financial management experience with Microdot, Inc.	64



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The executive officers of the Registrant are elected annually by the Board of Directors at its organizational meeting in May and hold office until the organizational meeting in the next year and until their respective successors are chosen and qualified.

### **Item 2. *Properties***

Lynch's principal executive offices in Providence, Rhode Island are leased and shared with Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto. Mr. Gabelli is Vice Chairman and a Director of Lynch. Mr. Papitto is Chairman and Chief Executive Officer of Lynch.

During 2000 Spinnaker moved its corporate headquarters from Dallas, Texas to Troy, Ohio, where it has major facilities.

Spinnaker Coating owns two manufacturing facilities, Plant One and Plant Two, in Troy, Ohio. Plant One is a 200,000 square foot complex and Plant Two is a 98,000 square foot facility. The facilities house manufacturing, administrative and shipping operations.

In connection with Spinnaker Coating's acquisition of the Warren facilities in March 1998, the parties entered into a site lease, which provides for Warren's lease of a portion of its Westbrook, Maine facility to Spinnaker. Such lease is for a term of 99 years, provides for nominal rent of \$1.00 per year, with an option to purchase for \$1.00. The facility contains approximately 50,000 square feet. With Spinnaker Coating's closure of its Maine business in July 2001, the facility is currently vacant and efforts are being made to sublease or sell the property. Spinnaker's plants are subject to security interests relating to its indebtedness.

Entoleter owns a manufacturing plant containing 72,000 square feet located on approximately 5 acres of land in Hamden, Connecticut. The land and building are subject to a mortgage and security agreement executed in support of a bank loan. Entoleter also owns approximately 6 unimproved acres located in Hamden, Connecticut adjacent to its property.

LS's operations are housed in two adjacent buildings situated on 3.19 acres of land in Bainbridge, Georgia. In January 1997, LS completed an expansion of its manufacturing capacity at this site, which added approximately 15,000 square feet, bringing total manufacturing space to approximately 73,000 square feet. Finished office area in the two buildings totals approximately 17,000 square feet. All such properties are subject to security deeds relating to loans.

Lynch-Amav located in Germany leases certain real and personal property under a commercial lease agreement that expires in December 2003. The lease agreement is between Lynch-Amav and the minority joint venture member's family and provides for annual lease payments of \$120,000.

M-tron's operations are housed in two separate facilities in Yankton, South Dakota. These facilities contain approximately 51,000 square feet in the aggregate. One facility owned by M-tron contains approximately 35,000 square feet and is situated on approximately 15 acres of land. The other Yankton facility containing approximately 16,000 square feet is leased, which lease expires on September 30, 2003, with options to extend the lease to 2006.

It is Registrant's opinion that the facilities referred to above are in good operating condition and suitable and adequate for present uses.

### **Item 3. *Legal Proceedings***

In the normal course of business subsidiaries of the Registrant are defendants in certain product liability, worker claims and other litigation in which the amounts being sought may exceed insurance coverage levels. The resolution of these matters is not expected to have a material adverse effect on the Registrant's

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consolidated financial condition or operations. In addition, Registrant and/or one or more of its subsidiaries are parties to the following additional legal proceedings:

**1. In re Spinnaker Coating, Inc., Debtor/ PACE Local 1-1069 v. Spinnaker Coating, Inc., and Lynch Corporation, U.S. Bankruptcy Court, District of Maine, Chapter 11, Adv. Pro. No. 02-2007; and PACE Local 1-1069 v. Spinnaker Industries, Inc., Spinnaker Coating, Inc., and Spinnaker Coating-Maine, Inc., Cumberland County Superior Court, CV-2001-00352:**

On or about June 26, 2001, in anticipation of the July 15, 2001 closure of Spinnaker's Westbrook, Maine facility, Plaintiff PACE Local 1-1069 filed a three count complaint in Cumberland County Superior Court, CV-2001-00352 naming the following defendants: Spinnaker Industries, Inc., Spinnaker Coating, Inc., and Spinnaker Coating-Maine, Inc. (collectively, the "Spinnaker Entities") and Lynch. The complaint alleged that under Maine's Severance Pay Act both the Spinnaker Entities and Lynch would be liable to pay approximately \$1,166,000 severance pay under Maine's Severance Pay Act in connection with the plant closure. The Defendants filed a notice of removal, thereby creating United States District Court Civil Action C.V. No. 01-236. The case was remanded to state court. The Spinnaker Entities also filed a separate complaint challenging the constitutionality of the Maine Severance Pay Act, United States District Court Civil Action No. 01-232. Thereafter, when the Spinnaker Defendants filed for relief under Chapter 11 of the Bankruptcy Code, they filed a second notice of removal, creating United States District Court for the District of Maine case number C.V. No. 02-7. Upon entry of an order confirming automatic reference, the C.V. No. 02-7 was referred to the United States Bankruptcy Court, District of Maine, and assigned Adv. Pro. No. 02-2007. This litigation was resolved as follows:

i) To the extent the United States District Court Civil Action No. 01-236 and 02-7 had not already been closed, the parties agreed to, as necessary, stipulations of dismissal disposing of those actions;

ii) The Spinnaker Entities stipulated to dismissal with prejudice, without costs, of United States District Court Civil Action No. 01-232;

iii) In Adv. Pro. No. 02-2007, Count I of the Plaintiff's complaint was dismissed with prejudice and without costs to any party;

iv) In Adv. Pro. No. 02-2007 Count III of the Plaintiff's complaint was dismissed without prejudice and without costs to any party;

v) In Adv. Pro. No. 02-2007 Count II of the Plaintiff's complaint was remanded to Cumberland County Superior Court, without costs and attorneys fees to any party. In consenting to remand, Lynch agreed that it would not challenge the subject matter jurisdiction of the Cumberland County Superior Court to conduct the trial and would not attempt to remove or otherwise invoke the jurisdiction of the federal court (except for appellate review to the extent permitted under applicable law), so long as the Plaintiff does not amend the complaint. Now Plaintiff's case will proceed against Lynch in Cumberland County Superior Court in Maine on the issue of whether Lynch has liability to Plaintiffs under the Maine Severance Pay Act. Lynch believes that, in addition to other defenses, it is not subject to the Maine Severance Pay Act, as now in effect, and will move for summary judgment. Management firmly believes that, under current law, the resolution of this case will not have a material adverse effect on the Registrant's consolidated financial condition or operations. Lynch has, however, become aware that plaintiff's counsel is sponsoring legislation to amend the Maine Severance Pay Act that, if enacted, could conceivably adversely affect the outcome of this case. At this time, management is unable to assess the prospects for enactment of any such legislation or, if enacted, how it might affect the outcome of this case.

**2. Spinnaker Chapter 11 Reorganization Proceeding**

On November 13, 2001 (the "Filing Date"), Spinnaker and its Spinnaker Coating, Spinnaker Coating-Maine, Inc. and Entoleter subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States

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Bankruptcy Code (11 U.S.C. §101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the “Court”). The cases are being jointly administered under Case No. 01-38066.

Effective December 28, 2001, Spinnaker’s Common Stock and Class A Common Stock were de-listed from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligation to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the “Letter of Intent”) with WR Capital Partners, LLC (“WR Capital”) whereby SP Acquisition LLC (“SP Acquisition”), an acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker’s (and its subsidiaries’) assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations). Entoleter’s assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement (as amended, the “Asset Purchase Agreement”) with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker’s assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker’s equity holders.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter’s assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 5, 2002. If the sale closes, Spinnaker estimates that pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter’s sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (i) and (ii), liquidate Entoleter’s assets.

### **3. Qui Tam Lawsuit**

Lynch Interactive Corporation (“Interactive”), Registrant and several other parties have been named as defendants in a lawsuit brought under the so-called “qui tam” provisions of the federal False Claims Act in the United States District Court for the District of Columbia. The complaint was filed under seal with the court on February 14, 2001. At the initiative of one of the defendants, the seal was lifted on January 11, 2002. Under the False Claims Act, a private plaintiff, termed a “relator,” may file a civil action on the U.S. government’s behalf against another party for violation of the statute. In return, the relator receives a statutory bounty from the government’s litigation proceeds if he is successful.

The relator in this lawsuit is R.C. Taylor III. The main allegation in the case is that the defendants participated in the creation of “sham” bidding entities that allegedly defrauded the federal Treasury by improperly participating in certain Federal Communications Commission spectrum auctions restricted to small businesses, as well as obtaining bidding credits in other spectrum auctions allocated to “small” and “very small” businesses. The lawsuit seeks to recover an unspecified amount of damages, which would be subject to mandatory trebling under the statute.

The U.S. Department of Justice has notified the court that it has declined to intervene in the case. The defendants strongly believe that this lawsuit is completely without merit and intend to defend the suit vigorously. Furthermore, Registrant believes that, under the separation agreement between Registrant and Interactive pursuant to which Interactive was spun off to Registrant’s shareholders on September 1, 1999, Interactive would be obligated to indemnify Registrant for any losses or damages incurred by Registrant as a result of this lawsuit. Nevertheless, Registrant cannot predict the ultimate outcome of the litigation, nor can

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Registrant predict the effect that the lawsuit or its outcome will have on Registrant's business or plan of operation. The defendants have yet to be formally served with the complaint.

### Item 4. *Submission of Matters to a Vote of Security Holders*

Not applicable.

## PART II

### Item 5. *Market for the Registrant's Common Equity and Related Stockholder Matters*

The Common Stock of Lynch Corporation is traded on the American Stock Exchange under the symbol "LGL." The market price highs and lows in consolidated trading of the Common Stock during the two years ended December 31, 2001 and 2000 are as follows:

	2001	Three Months Ended			
		March 31	June 30	September 30	December 31
High		42	30	34 6/8	23
Low		29	26	23	13
2000		March 31	June 30	September 30	December 31
High		33 1/2	32 7/8	51	50
Low		25 1/4	25 1/2	31 7/8	43

At March 15, 2002, the Company had 836 shareholders of record.

### Compliance with Listing Standards

On December 11, 2001 AMEX advised Lynch that it was initiating an informal review of Lynch's eligibility for continued listing on AMEX because, based upon AMEX's review of Lynch's Form 10-Q for the period ended September 30, 2001: (1) Lynch had shareholders equity of less than \$2 million and losses from continuing operations in two of its three most recent fiscal years and (2) Lynch had shareholders equity of less than \$4 million and losses in three out of its four most recent fiscal years. AMEX requested Lynch to provide the Exchange with Lynch's specific plan for achieving compliance with the Exchange's continued listing guidelines. On January 10, 2002, Lynch responded to the Exchange, explaining that Lynch's failure to meet the continued listing guidelines was attributable to the fact that, until September 30, 2001, by virtue of its control position in Spinnaker, Lynch was required to consolidate 100% of Spinnaker's losses and that, in the absence of these losses from Spinnaker, Lynch would have reported positive equity and positive net income for the 9-month period ending September 30, 2001. Lynch further explained that its new management team had taken steps to deconsolidate Spinnaker from Lynch for financial reporting purposes effective from and after September 30, 2001 by reducing Lynch's equity and voting interests in Spinnaker below 50%. See "Item 1. Business — C. Spinnaker — Deconsolidation". Lynch explained that the deconsolidation of Spinnaker resulted in a non-cash gain of \$27.4 million being recorded on September 30, 2001 and also resulted in Lynch retaining a negative investment in Spinnaker of \$19.4 million, representing Lynch's remaining interest in Spinnaker's accumulated deficit as of September 30, 2001; that this remaining interest represents losses in excess of investment, which has been recorded as a "deferred gain" on Lynch's balance sheet until such time as Spinnaker achieves profitability or Lynch disposes of its remaining interest in Spinnaker (see Note 1 to the Registrant's Consolidated Financial Statements included in this report); that Lynch will not record any additional losses from Spinnaker; that, in Lynch's view, the \$19.4 million "deferred gain" should be treated as equity by AMEX for purposes of assessing Lynch's compliance with the listing standards; and that, after giving effect to the deconsolidation of Spinnaker, Lynch retains a strong balance sheet. Finally, Lynch explained that management expects Lynch's business will be profitable and that the current negative equity position of Lynch, even before consideration of the aforementioned deferred gain as additional equity, would be reduced annually and turn positive in fiscal 2004.

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On January 29, 2002, the Exchange notified Lynch that it had determined to continue Lynch's listing pending a review of its March 31, 2002 Form 10-Q. The Exchange noted that, by then, Lynch should have made favorable progress towards regaining compliance with the listing guidelines. The Exchange further noted that its determination to continue Lynch's listing is subject to Lynch's favorable progress in satisfying the Exchange's guidelines for continued listing and to the Exchange's routine periodic reviews of Lynch's SEC filings. Finally, the Exchange requested a report on or before May 30, 2002 which provides (i) quarterly income statement, cash flow and balance sheet projections for the year ending December 31, 2002; (ii) a copy of Lynch's most recent business plan, if available; and (iii) an update on Lynch's stance with respect to its ownership position in Spinnaker.

The subsequent event described in Note 17 to the Consolidated Financial Statements should have a positive effect on Lynch's eligibility for continued listing.

## **Dividend Policy**

The Board of Directors has adopted a policy of not paying cash dividends, a policy which is reviewed annually. This policy takes into account the long term growth objectives of the Company, especially its acquisition program, shareholders' desire for capital appreciation of their holdings and the current tax law disincentives for corporate dividend distributions. Accordingly, no cash dividends have been paid since January 30, 1989 and none are expected to be paid in 2002. Substantially all of the subsidiaries' assets are restricted under the companies' current credit agreements and limit the companies' ability to pay dividends.

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Item 6. *Selected Financial Data*

**LYNCH CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SELECTED FINANCIAL DATA**  
**(Adjusted to Reflect Discontinued Operations and Spin Off of Lynch Interactive Corporation)**

(In thousands, except per share amounts)

	Year Ended December 31(a)				
	2001*	2000	1999	1998	1997
Revenues	\$141,073	\$219,196	\$194,222	\$187,644	\$153,735
Operating profit (loss)(b)	(19,240)	(4,977)	85	4,074	6,730
Net financial activities	(7,357)	(12,751)	(9,528)	(8,392)	(4,884)
Gain (loss) on sale of subsidiary stock and other operating assets	—	—	—	2,090	(91)
Income (loss) from continuing operations before income Taxes, minority interests, discontinued operations and Extraordinary items	(26,597)	(17,728)	(9,443)	(2,228)	1,755
(Provision) benefit for income taxes	(358)	2,793	2,544	1,408	(301)
Minority interests	4,017	9,252	2,647	1,107	(121)
Income (loss) from continuing operations before Discontinued operations and extraordinary items	(22,938)	(5,683)	(4,252)	287	1,333
Operations of Lynch Interactive Corporation(f)	—	—	(7,493)	4,929	(3,349)
Discontinued operations(c)	—	—	(572)	(1,859)	(862)
Gain on sale of Spinnaker's industrial tape Segment	—	—	10,431	—	—
Extraordinary items(d)	—	2,245	303	—	—
Net income (loss)	\$ (22,938)	\$ (3,438)	\$ (1,583)	\$ 3,357	\$ (2,878)
Per Common Share:(e)					
Income (loss) from continuing operations before Discontinued operations and extraordinary items:					
Basic	\$ (15.24)	\$ (3.81)	\$ (3.00)	\$ .20	\$ .94
Diluted	(15.24)	(3.81)	(3.00)	.20	.94
Net income (loss):					
Basic	(15.24)	(2.31)	(1.12)	2.37	(2.03)
Diluted	(15.24)	(2.31)	(1.12)	2.37	(2.03)
Cash, securities and short-term investments(g)	\$ 4,247	\$ 10,543	\$ 13,106	\$ 1,132	\$ 6,499
Restricted cash(g)(h)	4,703	6,500	56,026	—	—
Total assets (net of discontinued operations)(c)(f)(g)	32,091	162,820	211,192	251,658	183,720
Long-term debt, exclusive of current portion(g)	1,678	61,350	116,765	126,976	115,159
Shareholders' (deficiency) equity(f)(g)	(7,451)	15,432	15,991	11,441	14,464

**Notes:**

\* Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

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- (a) The data presented herein reflect the spin off of Lynch Interactive Corporation (Interactive) from the Company and the sale by Spinnaker Industries, Inc. (Spinnaker), of its industrial tape units, all of which transactions occurred in the third quarter of 1999. Accordingly, the operating results of both Interactive and the industrial tape segment have been segregated from continuing operations of the Company and are reported as separate line items. The data presented also includes results of the business acquired from S.D. Warren (name changed Spinnaker Coating-Maine, Inc.) from March 17, 1998, the date of its acquisition.
- (b) Operating profit (loss) is revenues less operating expenses, which excludes investment income, interest expense, extraordinary items, minority interests and taxes. Included are asset impairment and restructuring charges and the gain on deconsolidation (see Note g).
- (c) Discontinued operations of the industrial tape segment of Spinnaker Corporation. (See Note 3 to Financial Statements included elsewhere herein).
- (d) Gain on early extinguishments of debt at Spinnaker in 2000 and 1999.
- (e) Based on weighted average number of common shares outstanding.
- (f) No cash dividends have been declared over the period. In 1999 for each share of Lynch Common Stock, shareholders received one share of Lynch Interactive Corporation in a Spin Off of the multimedia and transportation business (See Note 4 to Financial Statements). In 1997, for each share of Lynch Common Stock, shareholders received one share of East/West Communications, Inc., an F block PCS licensee with licenses covering a population of 20 million.
- (g) 2001 excludes Spinnaker Industries as a result of the September 30, 2001 deconsolidation of Spinnaker resulting from the Company's disposition of shares of Spinnaker that reduced its ownership and voting interest of Spinnaker Industries, Inc. to 41.8% and 49.5% respectively.
- (h) See discussion of Restricted Cash in Note 6 — Notes Payable and Long-Term Debt included elsewhere herein.
- (i) For three year trend data of revenues and operating profit (loss) by segment, see Note 15-Segment Information.

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

#### **Critical Accounting Policies**

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in Item 8 of this Form 10-K. The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to the carrying value of inventories, realizability of outstanding accounts receivable, percentage of completion of long-term contracts, and the provision for income taxes. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. In the past, actual results have not been materially different from the Company's estimates. However, results may differ from these estimates under different assumptions or conditions.

The Company has identified the following as critical accounting policies, based on the significant judgments and estimates used in determining the amounts reported in its consolidated financial statements:

#### ***Accounts Receivable***

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The Company estimates potential losses based on its knowledge

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of the financial condition of certain customers. Historically, losses have been within the Company's expectations. If the financial condition of the Company's customers were to change, adjustments may be required to these estimates.

### ***Inventory Valuation***

The Company values its inventory at the lower of cost or market. If actual market conditions are more or less favorable than those projected by management, adjustments may be required.

### ***Accounting for Long-Term Contracts***

One of the Company's subsidiaries is engaged in the manufacture of machines and accounts for the related long-term contracts using the percentage-of-completion accounting method as costs are incurred. Estimates are used to determine the completion percentages and projected profitability of these contracts based on available information. Actual progress made on these contracts may result in future changes to these estimates.

### ***Income Taxes***

The carrying value of the Company's net deferred tax assets assumes that the Company will be able to generate sufficient future taxable income in certain tax jurisdictions to realize the value of these assets. If the Company is unable to generate sufficient future taxable income in these jurisdictions, an adjustment may be required to the net carrying value of the deferred tax assets resulting in additional income tax expense in the Company's consolidated statement of operations. Management evaluates the realizability of the deferred tax assets and assesses the need for any valuation adjustment quarterly.

### ***Recently Issued Accounting Standards***

The Company has described the impact anticipated from the adoption of certain new accounting pronouncements effective in 2002 in Note 1 to the consolidated financial statements included elsewhere herein.

## **Results of Operations**

### ***Year 2001 Compared to 2000 (including Results of Spinnaker for the nine months ended September 30, 2001)***

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and will prospectively account for its ownership of Spinnaker using the equity method of accounting. See Note 1 — "Basis of Presentation" included elsewhere herein. Accordingly, Spinnaker results of operations have only been included for nine months in 2001.

### ***Net Sales***

Revenues for the year ended December 31, 2001 were \$141.1 million, a reduction of \$78.1 million from Fiscal Year 2000. Spinnaker's net sales for the nine month period ending September 30, 2001 were \$93.4 million, compared to \$155.7 million for the full year in 2000. The decrease in Spinnaker net sales for 2001 was mainly attributable to lower selling prices due to excess capacity and depressed demand caused by the weakened general economy as well as the deconsolidation at September 30, 2001. Another contributing factor was the shutdown of Spinnaker's facility in Maine in the first quarter of 2001.

Lynch Systems' revenues increased by 10 percent to \$26.1 million due to increased order flow and sales of glass press machines used mainly by the producers of television and computer-monitor screens and other devices that incorporate electronic display. M-tron's served market, the infrastructure segment of the telecommunications industry, was deeply depressed by the major correction of overcapacity caused by the



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internet bubble. M-tron could not overcome the dramatic reduction in spending by its customers and suffered a sales decline from \$39.8 million in 2000 to \$21.6 million in 2001.

### *Operating Loss*

Operating loss for 2001 was \$19.2 million compared to an operating loss of \$5.0 million in 2000. Spinnaker's nine-month operating loss was \$47.3 million compared to an operating loss of \$9.5 million in 2000. Spinnaker's operating results primarily reflect lower operating margins due to lower selling prices attributable to excess capacity and a weak general economy. Spinnaker recognized restructuring charges affiliated with its Coating business, during the first nine months of 2001 of \$38.3 million compared to \$2.7 million in 2000. The 2001 restructuring charge was for the closing of the Spinnaker Coating facility in Westbrook, Maine. Non-cash asset impairment charges of \$36.8 million (goodwill \$20.8 million; fixed assets \$16.0 million) accounted for the majority of the \$38.3 million restructuring cost. The Company also recorded a \$27.4 million gain on deconsolidation of Spinnaker as discussed in Note 1 to the consolidated financial statements included elsewhere herein. Subsequent to the Company's deconsolidation of Spinnaker, Spinnaker filed for Chapter 11 bankruptcy protection in November, 2001. As of March 6, 2002, an agreement to sell the majority of the Spinnaker business had been approved by the bankruptcy court. See Note 17 to the consolidated financial statements included elsewhere herein for further details.

M-tron's operating profit declined by \$5.9 million from a profit of \$3.3 million to a loss of \$2.6 million. In spite of a 54 percent reduction in headcount and a further curtailment in hours worked, M-tron could not compensate for the 46 percent reduction in sales and lower selling prices. M-tron's 2000 and 2001 profits were also impacted by IPO/Rights offering costs of \$341,000 and \$266,000, respectively. M-tron's 2001 earnings were also reduced by a product issue with a long time contract manufacturer. M-tron provided reserves for this product issue totaling \$295,000 at December 31, 2001. In addition, M-tron wrote down its inventories by \$675,000 due to the sudden drop in demand that started in March, 2001. Lynch Systems operating profit increased by \$1.9 million to \$4.8 million due to increased order volume and cost controls that enabled Lynch Systems to improve its return on sales by 6 percentage points.

### *Other Income/Expense*

Investment income decreased by \$1.1 million (all attributable to Spinnaker) caused by lower investment earnings rates, the 9-month versus 12-month comparison, and less cash invested.

Interest expense of \$7.8 million was \$3.6 million less than the prior year primarily due to reduced debt at Lynch Systems, the 9-month versus 12-month comparison at Spinnaker, and lower borrowing rates.

Income tax benefit (expense) includes federal, state and local taxes. In spite of a net loss for the year 2001, there was a \$358,000 tax expense as Spinnaker's loss does not provide any tax benefits to Lynch. Factors resulting in this tax, and factors that reduced the year 2000 effective tax rate to 16% include provisions for contingencies, state income taxes, goodwill amortization, a valuation allowance for deferred taxes, and our foreign sales corporation.

Minority interests, reduced losses by \$4.0 million as a result of losses at Spinnaker that were allocable to the minority interests to the extent of their investment in Spinnaker, and profits of \$0.1 million for the minority interest in Lynch AMAV.

Net loss for the year ended December 31, 2001 was \$22.9 million, or (\$15.24) per share, which compares to the net loss of \$3.4 million, or (\$2.31) per share, for the same period of 2000, and was due primarily to Spinnaker's 9 month loss of \$54.5 million that was partly offset by the \$27.4 million gain on deconsolidation. See Note 1 to the consolidated financial statements included elsewhere herein.

Total backlog of manufactured products at December 31, 2001 (excluding Spinnaker) was \$13.4 million, which represents a decrease of \$12.5 million from the comparable backlog of \$25.9 million at December 31, 2000. Not included in this backlog is \$1.5 million and \$2.2 million at December 31, 2001 and 2000 respectively, representing a payment from a customer for a glass press order at Lynch Systems which was subsequently cancelled. The customer can use this amount for future orders and, if not utilized, will be

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forfeited to Lynch Systems. The backlog at Lynch Systems declined slightly from \$13.5 million to \$12.0 million. Meanwhile, the backlog at M-tron decreased to \$1.4 million from \$12.4 million due to the dramatic reduction in buying by OEM suppliers to the telecommunications sector which started in March, 2001.

### ***Year 2000 Compared to 1999***

#### ***Net Sales***

Revenues for the year ended December 31, 2000 were \$219.2 million, an increase of \$25.0 million from the comparable 1999 period. Spinnaker's 2000 net sales were \$155.7 million, compared to \$162.1 million in 1999. The decrease in net sales for 2000 is attributed to entering into a joint venture to outsource the manufacturing and sales of non-pressure sensitive product lines in the fourth quarter of 1999 and lower sales volumes of general purpose pressure-sensitive products. Net sales were also impacted by lower prices from intense price competition in the general purpose and other pressure-sensitive product lines. Offsetting these declines were increased sales of pressure-sensitive sheet products.

Additionally, net sales at Spinnaker's Entoleter business declined by \$1.4 million due to continued lower unit pricing. Revenues at M-tron increased by \$13.4 million due to increased demand from the telecommunications industry and increased sales of new products. Lynch Systems' revenues increased by \$18.0 million due to increased order flow and sales of glass press machines.

#### ***Operating Loss***

Operating loss for 2000 was \$5.0 million compared to an operating profit of \$.1 million in 1999. Spinnaker's operating loss was \$9.5 million compared to operating profit of \$1.6 million in 1999. Spinnaker's operating results primarily reflect lower operating margins, increased depreciation and amortization associated with capital expenditures used in the manufacturing process, lower product volumes, and an increase in product development costs. Spinnaker recognized certain restructuring charges, affiliated with its Coating business, during the fourth quarter 2000 of approximately \$2.2 million and had previously recorded approximately \$.5 million in the first quarter of 2000. To better concentrate on Coating's strengths and market niche, the decision was made by Spinnaker management to reorganize and realign the business in the fourth quarter of 2000 and going forward in 2001. The restructuring involved the elimination of product lines and related manufacturing operations, outsourcing of non-core manufacturing processes and the termination of seven salaried employees, primarily senior management.

M-tron's operating profit increased by \$1.4 million to \$3.3 million due to increased volume and increased margins. Lynch Systems operating profit increased by \$4.9 million to \$2.7 million due to increased order volume and a significant increase in margins over 1999 depressed levels.

#### ***Other Income/Expense***

Investment income decreased by \$.6 million due to the utilization of restricted cash from the 1999 sale of Spinnaker's industrial tape units to buy back debt which reduced the funds available for short-term investments.

Interest expense was \$11.4 million and decreased by \$.4 million from the prior year primarily due to the reduction of Spinnaker's Senior Notes by the repurchase mentioned above, offset by interest costs for short-term borrowings at various subsidiaries.

In addition, Spinnaker recognized an impairment loss of \$2.8 million in its investment in certain warrants as a result of the decline during the third and fourth quarter of 2000 in the underlying value of the stock associated with such warrants.

The income tax benefit includes federal, as well as state and local taxes. The tax benefit for the year ended December 31, 2000, and 1999, represents effective tax rates of 16% for 2000 and 27% for 1999. The

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differences from the federal statutory rate are principally due to the effect of state income taxes, foreign sales amortization of non-deductible goodwill and a valuation allowance on Spinnaker's deferred tax assets.

Minority interests contribution to the net income (loss) increased by \$6.6 million for the year from the prior year due to the increased losses from continuing operations at Spinnaker.

Net loss for the year ended December 31, 2000, was \$3.4 million, or (\$2.31) per share, which compares to the net loss of \$1.6 million, or (\$1.12) per share, for the same period of 1999, due primarily to the operating losses mentioned above, offset by Spinnaker's gain on repurchase of its Senior Notes (\$2.2 million after income taxes and minority interest).

### **Liquidity and Capital Resources (Excluding Spinnaker Industries)**

The discussion below excludes the impact of Spinnaker, which was deconsolidated at September 30, 2001 as discussed in Note 1 to the consolidated financial statements included elsewhere herein. Thus, the discussion below reflects liquidity and capital resource matters for the Company's remaining consolidated subsidiaries at December 31, 2001.

At December 31, 2001, the Company had current assets of \$25.9 million and current liabilities of \$16.3 million. Working capital was therefore \$9.6 million as compared to \$9.2 million at December 31, 2000. The ratio of current assets to current liabilities was 1.59 to 1.00 at December 31, 2001, an improvement over the 1.42 to 1.00 ratio at December 31, 2000.

Cash provided by operating activities was approximately \$8.4 million in 2001 compared to cash used of approximately \$2.9 million in 2000.

Capital expenditures, on a comparable basis, were \$0.6 million in 2001 and \$1.6 million in 2000. Capital expenditures in 2002 may return to the 2000 level of \$1.6 million. The Company anticipates that it will have sufficient cash flow from operations and borrowing availability under various credit facilities at the subsidiaries to fund such capital expenditures.

At December 31, 2001, total debt was \$3.3 million, which was \$2.3 million less than the \$5.6 million outstanding at the end of 2000. The reduction in debt is primarily due to reductions in the revolving credit loans. Debt outstanding at December 31, 2001 included \$940 thousand of fixed interest rate debt, at an 8.0% interest rate, and \$2.3 million of variable interest rate debt at a year end 2001 average rate of 5.0%. In May of 2001, Lynch Systems entered into an agreement with a bank for a \$4 million line of credit to be used only for the issuance of standby letters of credit. This line of credit is secured by accounts receivable and inventories. Amounts available under this line of credit will be used to fund letters of credit securing customer advances and certain warranty coverages. In August of 2001, M-tron entered into a credit agreement with its bank to set the line at \$6.2 million, including a \$5.0 million working capital line. In addition, the company has aggregate lease commitments of \$786,000. (See Note 14 to the Consolidated Financial Statements).

Lynch Systems has a February 2002 commitment from another bank to provide a \$6 million export/ import line, a \$2 million domestic revolving credit line, and a \$944 thousand term loan. Interest rates will be variable and currently would average about 4.6 percent. All of the new lenders' loan conditions have been met and the lender expects to close the loan by mid-April 2002. In the event the new loan is not closed, Lynch Systems would pursue other alternatives that could include funding by its parent, renewing the present bank line, and entering into a lending agreement with another financing source.

In 1987, the Board of Directors of Lynch authorized the repurchase of 400,000 common shares. As of December 31, 2001, Lynch's remaining authorization is to repurchase an additional 148,700 shares of common stock. On August 9, 2001, the Company purchased 12,300 shares of its Common Stock from a former director, Mr. Guzzetti, for a purchase price of \$396,204. Such purchase price was equal to the outstanding principal amount and unpaid interest on the loans made by the Company to Mr. Guzzetti on June 5, 2000 and September 20, 2000 to finance his original purchase of such Common Stock.

The Board of Directors has adopted a policy of not paying cash dividends, a policy which is reviewed annually. This policy takes into account the long term growth objectives of the Company, especially its

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acquisition program, shareholders' desire for capital appreciation of their holdings and the current tax law disincentives for corporate dividend distributions. Accordingly, no cash dividends have been paid since January 30, 1989 and none are expected to be paid in 2002. (See Note 6 to the Consolidated Financial Statements for restrictions on the companies assets).

### **Market Risk**

The Company is exposed to market risk relating to changes in the general level of U.S. interest rates. Changes in interest rates affect the amounts of interest earned on the Company's cash equivalents and short-term investments (approximately \$8.9 million at December 31, 2001). The Company generally finances the debt portion of the acquisition of long-term assets with fixed rate, long-term debt. The Company generally maintains the majority of its debt as fixed rate in nature by borrowing on a fixed long-term basis. The Company does not use derivative financial instruments for trading or speculative purposes. Management does not foresee any significant changes in the strategies used to manage interest rate risk in the near future, although the strategies may be reevaluated as market conditions dictate. There has been no significant change in market risk since December 31, 2001.

At December 31, 2001, approximately \$2.3 million of the Company's debt bears interest at variable rates. Accordingly, the Company's earnings and cash flows are slightly affected by changes in interest rates. Assuming the current level of borrowings for variable rate debt, and assuming a two percentage point increase in the 2001 average interest rate under these borrowings, it is estimated that the Company's interest expense would change by only \$0.1 million. In the event of an adverse change in interest rates, management would take actions to further mitigate its exposure.

### **Concentrations of Credit Risk**

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, investments, and trade accounts receivable.

The Company maintains cash and cash equivalents and short investments with various financial institutions. These financial institutions are located throughout the country and the Company's policy is designed to limit exposure to any one institution. The Company performs periodic evaluations of the relative credit standing of those financial institutions that are considered in the Company's investment strategy. Other than certain accounts receivable, the Company does not require collateral on these financial instruments. In relation to export sales, the Company requires letters of credit supporting a significant portion of the sales price prior to production to limit exposure to credit risk. The Company maintains an allowance for doubtful accounts at a level that management believes is sufficient to cover potential credit losses.

### **Risk Factors**

Certain subsidiaries and business segments of the Company sell to industries that are subject to cyclical economic changes. Any downturns in the economic environment would have a financial impact on the Company and its consolidated subsidiaries and may cause the reported financial information herein not to be indicative of future operating results, financial condition or cash flows.

Future activities and operating results may be adversely affected by fluctuating demand for capital goods such as large glass presses, delay in the recovery of demand for components used by telecommunications infrastructure manufacturers, disruption of foreign economies and the inability to renew or obtain new financing for expiring loans.

### **Item 7A. *Quantitative and Qualitative Disclosure About Market Risk***

The information required by this Item 7A is included under the caption "Market Risk" in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7.

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### **Item 8. *Financial Statements and Supplementary Data***

See Item 14(a).

### **Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

Not applicable.

## **PART III**

### **Item 10. *Directors and Executive Officers of the Registrant***

The information required by this Item 10 is included under the caption “Executive Officers of the Registrant” in Item 1 hereof and included under the captions “Election of Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is incorporated herein by reference.

### **Item 11. *Executive Compensation***

The information required by this Item 11 is included under the captions “Compensation of Directors,” “Executive Compensation,” “Executive Compensation and Benefits Committee Report on Executive Compensation” and “Performance Graph” in Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is incorporated herein by reference.

### **Item 12. *Security Ownership of Certain Beneficial Owners and Management***

The information required by this Item 12 is included under the caption “Security Ownership of Certain Beneficial Owners and Management,” in the Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is included herein by reference.

### **Item 13. *Certain Relationships and Related Transactions***

The information required by this Item 13 is included under the caption “Executive Compensation”, and “Transactions with Certain Affiliated Persons” in the Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is included herein by reference.

## **PART IV**

### **Item 14. *Exhibits, Financial Statements, Financial Statement Schedules and Reports on Form 8-K***

(a) The following documents are filed as part of this Form 10-K Annual Report:

(1) Financial Statements:

The Report of Independent Auditors and the following Consolidated Financial Statements of the Company are included herein:

Consolidated Balance Sheets at December 31, 2001 and 2000

Consolidated Statements of Operations — Years ended December 31, 2001, 2000 and 1999

Consolidated Statements of Shareholders’ Equity — Years ended December 31, 2001, 2000, and 1999

Consolidated Statements of Cash Flows — Years ended December 31, 2001, 2000, and 1999

Notes to Consolidated Financial Statements

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(2) Financial Statement Schedules as of December 31, 2001 and 2000 and for the three years ended December 31, 2001:

Schedule I — Condensed Financial Information of Registrant

Schedule II — Valuation and Qualifying Accounts

All other schedules for which provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions, or are inapplicable, and therefore have been omitted.

See Page 2 above re Forward Looking Information.

(b) Reports on Form 8-K: None

(c) The following Exhibits listed in the Exhibit Index are filed with this Form 10-K Annual Report:

2(a) — Asset Purchase Agreement (“Asset Purchase Agreement”), dated January 18, 2002, by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and SP Acquisition, LLC.

2(b) — Asset Purchase Agreement Amendment No. 1 dated February 15, 2002.

2(c) — Asset Purchase Agreement Amendment No. 2 dated February 25, 2002.

2(d) — Asset Purchase Agreement Amendment No. 3 dated March 5, 2002.

2(e) — Asset Purchase Agreement Amendment No. 4 dated March 8, 2002.

2(f) — Asset Purchase Agreement Amendment No. 5 dated March 18, 2002.

2(g) — Schedules to Asset Purchase Agreement dated January 18, 2002.

2(h) — United States Bankruptcy Court Order dated March 6, 2002; In Re: Spinnaker Industries, Inc., et al., C.A. No. 01-38066.

10(x) — Amendment dated February 7, 2002 among Registrant, Mario J. Gabelli and Ralph R. Papitto, amending the Agreement at Exhibit 10(w) to terminate Registrant’s obligation to grant an option to Mr. Papitto.

10(y) — Registrant’s 2001 Equity Incentive Plan adopted December 10, 2001.

21 — Subsidiaries of the Registrant.

23 — Consent of Ernst & Young LLP.

24 — Powers of Attorney.

(d) Financial Statement Schedules:

Financial Statement Schedules are listed in response to Item 14(a)(2)

**REPORT OF INDEPENDENT AUDITORS**

Shareholders and Board of Directors  
Lynch Corporation

We have audited the accompanying consolidated balance sheets of Lynch Corporation and subsidiaries (“Lynch Corporation” or the “Company”) as of December 31, 2001 and 2000, and the related consolidated statements of operations, shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2001. Our audits also included the financial statement schedules listed in the index at Item 14(a). These financial statements and schedules are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lynch Corporation and subsidiaries at December 31, 2001 and 2000 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statements schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects, the information set forth therein.

/s/ ERNST & YOUNG LLP

Stamford, Connecticut  
March 29, 2002

LYNCH CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31, 2001	December 31, 2000
(In thousands, except share amounts)		
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 4,247	\$ 10,543
Restricted cash (Note 1)	4,703	6,500
Trade accounts receivable, less allowances of \$118 and \$1,582, respectively	9,818	35,019
Inventories	5,260	35,139
Deferred income taxes	988	7,624
Prepaid expense	836	1,807
<b>Total Current Assets</b>	<b>25,852</b>	<b>96,632</b>
Property, Plant and Equipment		
Land	291	797
Buildings and improvements	4,158	11,076
Machinery and equipment	11,949	56,951
	16,398	68,824
Less: Accumulated depreciation	(10,942)	(27,713)
	5,456	41,111
Excess of cost over fair value of net assets acquired, net	—	21,589
Other assets	537	3,488
<b>Total Assets</b>	<b>\$ 31,845</b>	<b>\$162,820</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Notes payable to banks	\$ 1,086	\$ 30,288
Trade accounts payable	1,717	19,251
Accrued interest payable	7	1,185
Accrued liabilities	6,189	15,234
Customer advances	6,781	3,916
Current maturities of long-term debt	521	1,376
<b>Total Current Liabilities</b>	<b>16,301</b>	<b>71,250</b>
Long-term debt	1,678	61,350
Deferred income taxes	578	6,752
Other long-term liabilities	1,319	3,908
Minority interests	—	4,128
<b>Total Liabilities</b>	<b>19,876</b>	<b>147,388</b>
Loss in Excess of Investment (Note 1)	19,420	—
Comments and Contingencies (Note 14)		
Shareholders' (Deficiency) Equity		
Common stock, no par or stated value — 10,000,000 shares Authorized; 1,513,191 shares issued; 1,497,883 and 1,510,183 shares outstanding	5,139	5,139
Additional paid-in capital	10,403	10,403
(Accumulated deficit) retained earnings	(22,533)	405
Officer's note receivable	—	(382)
Accumulated other comprehensive loss	(2)	(71)
Treasury stock of 15,308 and 3,008 shares at cost	(458)	(62)
<b>Total Shareholders' (Deficiency) Equity</b>	<b>(7,451)</b>	<b>15,432</b>
<b>Total Liabilities and Shareholders' (Deficiency) Equity</b>	<b>\$ 31,845</b>	<b>\$162,820</b>

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.



LYNCH CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

	Years ended December 31,		
	2001	2000	1999
	(In thousands, except share and per-share amounts)		
SALES AND REVENUES	\$ 141,073	\$ 219,196	\$ 194,222
Costs and expenses:			
Manufacturing cost of sales	130,290	192,980	172,567
Selling and administrative	19,157	28,485	21,120
Asset impairment and restructuring charges	38,272	2,708	450
	187,719	224,173	194,137
Gain on deconsolidation (Note 1)	27,406	—	—
OPERATING PROFIT (LOSS)	(19,240)	(4,977)	85
Other income (expense):			
Investment income	384	1,481	2,354
Interest expense	(7,741)	(11,432)	(11,882)
Impairment of Spinnaker's investment in warrants	—	(2,800)	—
	(7,357)	(12,751)	(9,528)
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES, MINORITY INTERESTS, DISCONTINUED OPERATIONS AND EXTRAORDINARY ITEM	(26,597)	(17,728)	(9,443)
(Provision) Benefit for income taxes	(358)	2,793	2,544
Minority interests	4,017	9,252	2,647
LOSS FROM CONTINUING OPERATIONS BEFORE DISCONTINUED OPERATIONS AND EXTRAORDINARY ITEM	(22,938)	(5,683)	(4,252)
DISCONTINUED OPERATIONS:			
Loss from operations of Lynch Interactive Corporation distributed to shareholders (less income tax benefit of \$3,068 and minority interests of \$578)	—	—	(7,493)
Loss from discontinued operations of industrial tape segment of Spinnaker Industries (less applicable income tax benefit of \$308 and minority interests of \$558)	—	—	(572)
Gain on sale of Spinnaker's industrial tape operations (less income tax provision of \$6,495 and minority interest of \$7,013)	—	—	10,431
EXTRAORDINARY ITEM:			
Gain on early extinguishments of debt (less income tax provision of \$2,612 and \$355 and minority interest of \$2,472 and \$300)	—	2,245	303
NET LOSS	\$ (22,938)	\$ (3,438)	\$ (1,583)
Weighted average shares outstanding	1,505,300	1,491,000	1,415,000
Basic and diluted loss per share:			
Loss from continuing operations before discontinued operations	\$ (15.24)	\$ (3.81)	\$ (3.00)
Loss from Lynch Interactive Corporation	—	—	(5.30)
Income from discontinued operations	—	—	6.97
Extraordinary item	—	1.51	.21
NET LOSS	\$ (15.24)	\$ (2.30)	\$ (1.12)

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

See accompanying notes

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**LYNCH CORPORATION AND SUBSIDIARIES**  
**Consolidated Statements of Shareholders' Equity**  
**For the Three Years Ended December 31, 2001**

	Shares of Common Stock Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Officer's Note Receivable	Accumulated Other Comprehensive Income	Treasury Stock	Total
(In thousands except for shares of common stock)								
BALANCE AT DEC. 31, 1998	1,418,248	5,139	8,554	26,771	\$ 0	59	(730)	39,793
Comprehensive Income (Loss):								
Net loss for year	—	—	—	(1,583)	—	—	—	(1,583)
Other comprehensive income (loss)	—	—	—	—	—	(40)	—	(40)
Comprehensive Income (Loss)								(1,623)
Purchase of Treasury Stock	(8,065)	—	—	—	—	—	(523)	(523)
Capital transactions of The Morgan Group, Inc.	—	—	(252)	—	—	—	—	(252)
Dividend of Lynch Interactive Corporation	—	—	—	(21,345)	—	(59)	—	(21,404)
BALANCE AT DEC. 31, 1999	1,410,183	5,139	8,302	3,843	\$ 0	(40)	(1,253)	15,991
Comprehensive Income (Loss):								
Net loss for year	—	—	—	(3,438)	—	—	—	(3,438)
Other comprehensive income (loss)	—	—	—	—	—	(31)	—	(31)
Comprehensive Income (Loss)								(3,469)
Issuance of Common Stock	100,000	—	1,809	—	—	—	1,191	3,000
Capital transactions of Lynch Systems	—	—	292	—	—	—	—	292
Loan to Officer to buy Common stock	—	—	—	—	(382)	—	—	(382)
BALANCE AT DEC. 31, 2000	1,510,183	\$5,139	\$10,403	\$ 405	(\$ 382)	\$(71)	\$ (62)	\$ 15,432
Comprehensive Income (Loss):								
Net loss for year	—	—	—	(22,938)	—	—	—	(22,938)
Other comprehensive income	—	—	—	—	—	69	—	69
Comprehensive Income (Loss)								(22,869)
Acquisition of Treasury Stock	(12,300)	—	—	—	382	—	(396)	(14)
BALANCE AT DEC. 31, 2001	1,497,883	\$5,139	\$10,403	\$(22,533)	\$ —	\$ (2)	(458)	\$ (7,451)

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

*See accompanying notes.*

**LYNCH CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Years Ended December 31,		
	2001	2000	1999
	(In thousands)		
<b>OPERATING ACTIVITIES</b>			
Net loss	\$(22,938)	\$ (3,438)	\$ (1,583)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities of continuing operations:			
Gain on deconsolidation	(27,406)	—	—
Loss on donation of shares	366	—	—
Asset impairment and restructuring charges	38,272	—	—
Extraordinary item, net	—	(2,245)	(303)
Depreciation	4,315	6,734	5,147
Amortization of goodwill and other assets	244	1,001	1,087
Amortization of deferred financing charges	703	876	786
Deferred taxes	501	1,846	(2,719)
Minority interests	(4,017)	(7,072)	(2,636)
Other	761	2,800	(854)
Adjustment from discontinued operations:			
Loss from operations of Lynch Interactive Corporation	—	—	7,493
Loss from operations of industrial tape segment	—	—	572
Gain on sale of industrial tape segment	—	—	(10,431)
Changes in operating assets and liabilities:			
Receivables	10,861	(10,377)	678
Inventories	13,430	(3,459)	(3,284)
Accounts payable and accrued liabilities	(14,269)	10,112	(3,949)
Other Assets/ Liabilities	4,727	(212)	864
Net cash provided by (used in) operating activities of continuing operations	5,550	(3,434)	(9,132)
<b>INVESTING ACTIVITIES</b>			
Capital Expenditures	(1,104)	(4,323)	(3,795)
Restricted Cash	1,797	49,526	(56,026)
Reduction in cash due to deconsolidation	(5,728)	—	—
Proceeds from sale of industrial tape segment	—	—	104,450
Proceeds from sale of fixed assets	—	—	2,403
Other	(860)	(767)	509
Net cash provided by (used in) investing activities of continuing operations	(5,895)	44,436	47,541
<b>FINANCING ACTIVITIES</b>			
Net borrowings (repayments) of notes payable	(7,587)	7,110	(36,127)
Repayment of long-term debt	(420)	(53,433)	(10,937)
Proceeds from long-term debt	1,987	—	—
(Purchase) sale of treasury stock	—	1,191	(523)
Issuance of common stock	—	1,809	—
Other	69	(242)	(580)
Net cash used in financing activities of continuing operations	(5,951)	(43,565)	(48,167)
Net decrease in cash and cash equivalents	(6,296)	(2,563)	(9,758)
Cash provided by Lynch Interactive Corporation	—	—	15,987
Cash provided by industrial tape segment	—	—	5,745
Increase (decrease) in cash and cash equivalents	(6,296)	(2,563)	11,974
Cash and cash equivalents at beginning of year	10,543	13,106	1,132
Cash and cash equivalents at end of year	\$ 4,247	\$ 10,543	\$ 13,106

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

*See accompanying notes*

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2001**

**1. Accounting and Reporting Policies**

*Organization*

Lynch Corporation is a diversified holding company with subsidiaries engaged in manufacturing primarily in the United States. The Company has two wholly-owned subsidiaries (Lynch Systems, Inc. and M-tron Industries, Inc.) and an investment in Spinnaker Industries, Inc. (“Spinnaker”) accounted for under the equity method of accounting; see discussion below. Information on the Company’s operations by segment and geographic area is included in Note 15 — Segment Information.

*Basis of Presentation*

Prior to September 30, 2001, the Company owned 47.6% of the equity of Spinnaker (60.4% voting control), an entity engaged in the manufacture of adhesive-backed material; as such, under accounting principles generally accepted in the United States, Spinnaker was a consolidated entity and the Company was required to record all of the losses of Spinnaker since the non-Company interests were not required to absorb their share of the losses (52.4%) after their investment was fully absorbed by losses (which occurred in the first quarter of 2001).

Effective September 30, 2001, the Company donated 430,000 shares of Spinnaker Class A common stock to a university on whose board several of the Company’s executives serve as Trustees, thereby relinquishing control of such securities. This resulted in the reduction of the Company’s ownership and voting interests in Spinnaker to 41.8% and 49.5%, respectively. As a result, effective September 30, 2001, the Company deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting.

Accordingly, the Company’s results of operations include the operating results of Spinnaker through September 30, 2001 (date of deconsolidation). The balance sheet at December 31, 2001 does not contain the assets and liabilities of Spinnaker due to the deconsolidation. This deconsolidation resulted in a non-cash gain of \$27,406,000 being recorded on September 30, 2001 to reduce the Company’s negative investment in Spinnaker to \$19,420,000, which represents the Company’s interest in Spinnaker’s accumulated deficit at the date of deconsolidation. This remaining interest represents losses in excess of investment, which has been recorded as a deferred credit on the Company’s balance sheet until such time as Spinnaker achieves profitability or the Company disposes of its remaining interests in Spinnaker. The Company will not record any additional losses from Spinnaker as the Company has no further obligations to Spinnaker (see Note 17).

The following summarized balance sheet information of Spinnaker is presented as follows at September 30, 2001 (date of deconsolidation) and December 31, 2000):

	(unaudited) September 30, 2001	December 31, 2000
Current Assets	\$ 36,881	\$ 59,496
Total Assets	54,902	119,031
Current Liabilities	38,759	49,409
Long-Term Debt	61,239	60,310
Shareholder’s Deficit	(46,460)	(7,468)

*Principles of Consolidation*

The consolidated financial statements include the accounts of Lynch Corporation (the “Company” or “Lynch”) and entities in which Lynch had majority voting control. All material intercompany transactions

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

and accounts have been eliminated in consolidation. See Note 4 for details of the spin off of Lynch Interactive Corporation, which occurred on September 1, 1999.

*Uses of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

*Cash Equivalents*

Cash equivalents consist of highly liquid investments with a maturity of less than three months when purchased.

At December 31, 2001 and 2000, assets of \$2.1 million and \$8.7 million, which are classified as cash and cash equivalents, are invested in United States Treasury money market funds for which affiliates of the Company serve as investment managers to the respective funds.

*Restricted Cash*

At December 31, 2001 and 2000, the Company had \$4.7 million and \$6.5 million of Restricted Cash. (See Note 6.)

*Accounts Receivable*

Accounts receivable on a consolidated basis consist principally of amounts due from both domestic and foreign customers. Credit is extended based on an evaluation of the customer's financial condition and collateral is not generally required except at Lynch Systems (See discussion of Accounting for Long Term Contracts below). The Company considers concentrations of credit risk to be minimal due to the Company's diverse customer base. In relation to export sales, the Company requires letters of credit supporting a significant portion of the sales price prior to production to limit exposure to credit risk. Certain subsidiaries and business segments have credit sales to industries that are subject to cyclical economic changes. The Company maintains an allowance for doubtful accounts at a level that management believes is sufficient to cover potential credit losses.

*Property, Plant and Equipment, Net*

Property, plant and equipment are recorded at cost less accumulated depreciation and include expenditures for additions and major improvements. Maintenance and repairs are charged to operations as incurred. Depreciation is computed for financial reporting purposes using the straight-line method over the estimated useful lives of the assets, which range from 5 years to 35 years for buildings and for 3 to 10 years for other fixed assets. For income tax purposes, accelerated depreciation methods are used.

*Excess of Cost over Fair Value of Net Assets Acquired, Net*

As of December 31, 2001, there is no goodwill on the books of Lynch Corporation. The majority of goodwill on Spinnaker books at December 31, 2000 (\$20.8 million) was written-off in 2001 and is included in asset impairment and restructuring charges in the statements of operations (See Note 2).

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

***Revenue Recognition***

Revenues, with the exception of certain long-term contracts discussed below, are recognized on shipment. Shipping costs are included in manufacturing cost of sales.

***Accounting for Long-Term Contracts***

Lynch Systems, a 100% owned subsidiary of the Company, is engaged in the manufacture and marketing of glass-forming machines and specialized manufacturing machines. Certain sales contracts require an advance payment (usually 30% of the contract price) which is accounted for as a customer advance. The contractual sales prices are paid either (i) as the manufacturing process reaches specified levels of completion or (ii) based on the shipment date. Guarantees by letter of credit from a qualifying financial institution are required for most sales contracts. Because of the specialized nature of these machines and the period of time needed to complete production and shipping, Lynch Systems accounts for these contracts using the percentage-of-completion accounting method as costs are incurred (cost to cost basis). At December 31, 2001 and 2000, costs and estimated earnings in excess of billings (included in accounts receivable) were \$5.3 million and \$2.7 million, respectively.

***Research and Development Costs***

Research and development costs are charged to operations as incurred. Such costs were \$1,772,000, \$1,603,000, and \$1,386,000 in 2001, 2000, and 1999, respectively.

***Advertising Expense***

The cost of advertising is expensed as incurred. The Company incurred \$177,000, \$472,000, and \$340,000 in advertising costs during 2001, 2000 and 1999, respectively.

***Earnings Per Share***

The Company's basic and diluted earnings per share are equivalent as the Company has no dilutive securities (see Note 9).

***Segment Information***

The Company reports segment information in accordance with Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information" (SFAS 131). SFAS No. 131 requires companies to report financial and descriptive information for each operating segment based on management's internal organizational decision-making structure. See Note 15 for the detailed presentation of business segments report.

***Impairments***

The Company accounts for impairments of long-lived assets in accordance with the provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Assets to be Disposed Of". The Company periodically assesses the net realizable value of its long-lived assets and evaluates such assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. For assets to be held and used, impairment is determined to exist if estimated undiscounted future cash flows are less than the carrying amount. For assets to be disposed of, impairment is determined to exist if the estimated net realizable value is less than the carrying amount. If indicators of impairment are present, and we do not expect the estimated undiscounted cash flows to be derived from the related assets to be sufficient to recover the asset's carrying amount, an impairment loss is charged to expense in the period identified based upon the difference between the carrying amount and the discounted cash flows. The rates

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

that would be utilized to discount the net cash flows to net present value would take into account the time value of money and investment risk factors. See Note 2 regarding Spinnaker's restructuring costs for fiscal years 2001 and 2000.

***Stock Based Compensation***

The Company grants stock options for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant. The Company accounts for stock option grants in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25) and related Interpretations because the Company believes the alternative fair value accounting provided for under FASB Statement No. 123, *Accounting for Stock-Based Compensation*, (FAS 123) requires the use of option valuation models that were not developed for use in valuing employee stock options.

***Financial Instruments***

Cash and cash equivalents, trade accounts receivable, short-term borrowings, trade accounts payable and accrued liabilities are carried at cost which approximates fair value due to the short-term maturity of these instruments. The carrying account of the Company's borrowings under its revolving lines of credit approximates fair value, as the obligations bear interest at a floating rate. The fair value of other long-term obligations approximates cost based on borrowing rates for similar instruments.

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, investments, trade accounts receivable.

The Company maintains cash and cash equivalents and short-term investments with various financial institutions. These financial institutions are located throughout the country and the Company's policy is designed to limit exposure to any one institution. The Company performs periodic evaluations of the relative credit standing of those financial institutions that are considered in the Company's investment strategy. Other than certain accounts receivable, the Company does not require collateral on these financial instruments.

***Issuance of Stock by Subsidiaries and Investees***

Changes in the Company's equity in a subsidiary or an investee caused by issuance of the subsidiary's or investees' stock are accounted for as gains or losses where such issuance is not part of a broader reorganization (see Note 10).

***Reclassifications***

The consolidated financial statements reflect the spin off of Lynch Interactive Corporation (Interactive) from Lynch Corporation that occurred in the third quarter of 1999 and also the sale by Spinnaker Industries, Inc. (Spinnaker), of its two industrial tape units, Central Products Company and Spinnaker Electrical that also occurred in the third quarter of 1999.

Accordingly, the operating results of both Interactive and the industrial tape segment have been segregated from continuing operations of the Company and are reported as separate line items on the financial statements as discontinued operations.

Certain other amounts in the 2000 and 1999 financial statements have been reclassified to conform to the 2001 presentation. These other reclassifications are immaterial to the consolidated financial statements taken as a whole.

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

*Recent Issued Accounting Pronouncements*

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 141, “Business Combinations” (“FAS 141”), and Statement of Financial Accounting Standards No. 142, “Goodwill and Other Intangible Assets” (“FAS 142”). FAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. FAS 141 also includes guidance on the initial recognition and measurement of goodwill and intangible assets arising from business combinations completed after June 30, 2001. FAS 142 requires that these assets be reviewed for impairment at least annually. Intangible assets with finite lives will continue to be amortized over their estimated useful lives. Additionally, FAS 142 requires that goodwill included in the carrying value of equity method investments no longer be amortized.

The Company will apply FAS 142 beginning in the first quarter of 2002. The Company will test indefinite-lived intangible assets for impairment using the two-step process prescribed by FAS 142. The first step is a screen for potential impairment, while the second step measures the amount of impairment, if any. The Company expects to perform the first of the required impairment tests of indefinite-lived intangible assets as of January 1, 2002 in the first quarter of 2002. Any impairment charge resulting from these transitional impairment tests will be reflected as the cumulative effect of a change in accounting principles in the first quarter of 2002. The Company does not anticipate that the effect of these tests will be material to the earnings and financial position of the Company.

In August 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets” (“FAS 144”), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes Statement of Financial Accounting Standards No. 121, “Accounting for the Impairment of Long-Lived Assets to be Disposed Of”, and the accounting and reporting provisions of APB Opinion No. 30, “Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequent Occurring Events and Transactions”. FAS 144 is effective for fiscal years beginning after December 15, 2001. The Company will adopt FAS 144 as of January 1, 2002 and it does not expect that the adoption of the Statement will have a significant impact on the Company’s financial position or results of operations.

**2. Asset Impairment and Restructuring Charges**

Prior to the deconsolidation of Spinnaker on September 30, 2001 (see Note 1), the Company recognized certain restructuring charges in 2001 related to Spinnaker, totaling \$41.8 million. The charges resulted from (a) the write-down to estimated fair market value of fixed assets to be taken out of service and held for sale or disposal; (b) impairment of goodwill associated with the acquisition of Coating — Maine in 1998; (c) severance and related costs; and (d) inventory write-downs of \$3.5 million (recorded through manufacturing costs of sales).

To better concentrate on Coating’s strengths and market niche, a decision was made by Spinnaker’s management to reorganize and realign the business in the fourth quarter of 2000. Spinnaker recognized certain restructuring charges, primarily affiliated with its Spinnaker Coating and Spinnaker Coating — Maine businesses, in 2000 of approximately \$2.7 million.

**3. Discontinued Operations**

On April 9, 1999, Spinnaker entered into a definitive agreement to sell its industrial tape segment to Intertape Polymer Group, Inc. for approximately \$105 million and five-year warrants to purchase 300,000 shares of Intertape common stock (New York Stock Exchange Symbol “ITP”) at an exercise price of \$29.50 per share. At the time, the warrants were valued at approximately \$3.0 million using the Black-Scholes option



**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

pricing model. At December 31, 2000, the fair value of the warrants was approximately \$0.2 million, accordingly, in accordance with SFAS No. 121, Spinnaker recognized an impairment loss of \$2.8 million as a result of the decline during the third and fourth quarters of 2000 in the market value of the stock associated with the warrants which are recorded in other assets.

The sale of the two industrial tape businesses closed on August 10, 1999 and July 30, 1999. Accordingly, operating results of the industrial tape segment have been segregated from continuing operations and reported as a separate line item in the statements of operations. The Company recorded gains totaling \$17.4 million, net of applicable income taxes of approximately \$6.5 million. Spinnaker offset the cash tax liability by utilizing net operating loss carry forwards. The industrial tape segments net sales were \$69.5 million in the period ended December 31, 1999 (through the date of sale).

General corporate office expenses related to finance and administrative functions including public company compliance reporting, bank and investor relations, taxes other than income taxes and holding company payroll, historically allocated and charged to the industrial tape segment were reversed and allocated back to continuing operations. These expenses were not considered to be directly attributed to discontinued operations. Historical expenses allocated back to continuing operations totaled \$1.0 million for the period ended December 31, 1999.

Interest expense attributed to the Spinnaker senior notes and related deferred financing had historically been allocated based on the pro rata share of subsidiary debt obligations retired with the proceeds from the issuance of the senior notes, to total debt obligations retired. The senior note proceeds were used to extinguish certain outstanding term and revolver obligations in October 1996. Interest expense charged to the discontinued industrial tape segment totaled \$5.2 million for the period ended December 31, 1999.

**4. Spin Off**

On August 12, 1999, the Board of Directors approved a plan to distribute the stock of Lynch Interactive Corporation on a one for one basis to the shareholders of Lynch Corporation (“spin off”). Lynch completed the spin off of Lynch Interactive Corporation (“Interactive”) on September 1, 1999, to stockholders of record on August 23, 1999. Pursuant to the spin off, each Lynch shareholder received one share of Interactive common stock for each share of Lynch owned. Lynch had received a private letter ruling from the Internal Revenue Service that the spin off would be tax free to Lynch shareholders. Interactive is listed on the American Stock Exchange under the symbol “LIC”.

Interactive owns all of what were Lynch’s multimedia and service businesses while Lynch retained the manufacturing businesses. Interactive owns the telephone companies, television interests and PCS interests, as well as the 55% equity interest of The Morgan Group, Inc. In addition, Interactive owns a 13.6% equity interest in Spinnaker Industries, Inc. In the third quarter of 1999, Lynch acquired by merger, all of the stock of Central Scott Telephone Company. This company became part of Lynch Interactive and was included in the spin off.

As a result, the Company’s multimedia and services segments are being reported as operations distributed to shareholders in the accompanying consolidated financial statements. Accordingly, operating results of Lynch Interactive Corporation for 1999 have been segregated from continuing operations and reported as a separate line item on the statements of operations. Interactive’s net sales were \$ 204.6 million for the fiscal year ended December 31, 1999.

Lynch Interactive and Lynch have entered into certain agreements governing various ongoing relationships, including the provision of support services and a tax allocation agreement. The tax allocation agreement provides for the allocation of tax attributes to each company as if it had actually filed with the respective tax authority. At the spin off, the employees of the corporate office of Lynch Corporation became the employees of Lynch Interactive Corporation and Lynch Interactive Corporation began providing certain support services

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

to Lynch. The Company was charged a management fee for these services amounting to approximately \$180,000, \$265,000 and \$200,000 in 2001, 2000 and 1999, respectively. Note that this arrangement was terminated in August, 2001.

The net assets distributed to Interactive were estimated to be \$22.6 million at September 1, 1999. Such amount was subsequently decreased in the fourth quarter by \$1.6 million to reflect revised estimates of liabilities distributed.

**5. Inventories**

Inventories are stated at the lower of cost or market value. Inventories valued using the last-in, first-out (LIFO) method comprised approximately 20% (which excluded Spinnaker due to the deconsolidation discussed in Note 1) and 28% of consolidated inventories at December 31, 2001 and 2000, respectively. The balance of inventories at December 31, 2001 are valued using the first-in-first-out (FIFO) method. At December 31, 2000, the balance of inventories were valued using the FIFO method and specific identification method (for Spinnaker).

	December 31,	
	2001	2000
	(In Thousands)	
Raw materials and supplies	\$1,844	\$10,172
Work in progress	2,003	2,796
Finished goods	1,413	22,171
Total	<u>\$5,260</u>	<u>\$35,139</u>

Current cost exceeded the LIFO value of inventories by \$991,000 and \$966,000 at December 31, 2001 and 2000, respectively.

**6. Notes Payable to Banks and Long-term Debt**

Notes payable to banks and long-term debt consists of:

	December 31,	
	2001	2000
	(In Thousands)	
Notes payable:		
M-tron bank revolving loan at variable interest rates (4.5% at December 31, 2001), due May 2002	\$1,086	\$ 3,004
Lynch Systems bank revolving loan at variable interest rates, due August 2002	—	1,150
Spinnaker notes payable with variable interest rates	—	26,134
	<u>\$1,086</u>	<u>\$30,288</u>
Long-term debt:		
M-tron term loan at variable interest rates (5.0% at December 31, 2001), due September 2004	\$1,259	\$ —
Lynch Systems term loan at a fixed interest rate of 8.0%, due August 2003	607	635
Spinnaker 10.75% senior secured notes, due 2006	—	51,135
Spinnaker subordinated note at a fixed interest rate of 14%, due 2003	—	9,172
Other debt	333	1,784
	<u>2,199</u>	<u>62,726</u>
Current maturities	(521)	(1,376)
	<u>\$1,678</u>	<u>\$61,350</u>

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

On a consolidated basis, at December 31, 2001, Lynch maintains short-term and long-term line of credit facilities totaling \$10.2 million, of which \$5.9 million was available for future borrowings. These facilities generally limit the credit available under the lines of credit to certain variables, such as inventories and receivables, and are secured by the operating assets of the respective subsidiary borrower, and include various financial covenants which currently restrict the transfer of substantially all the assets of the subsidiaries. At December 31, 2001, all of these facilities expire within one year. The weighted average interest rate for short-term borrowings at December 31, 2001 and 2000 was 5.0% and 9.5%, respectively. In May of 2001, Lynch Systems entered into an agreement with a bank for a \$4 million line of credit to be used only for the issuance of standby letters of credit. This line of credit is secured by accounts receivable and inventories. Amounts available under this line of credit will be used to fund letters of credit securing customer advances and certain warranty coverages. Cash of \$4.7 million at December 31, 2001 has been disclosed as restricted as required under certain letters of credit outstanding. Total letters of credit outstanding at December 31, 2001 totaled \$7.9 million. In August of 2001, M-tron entered into a credit agreement with its bank to set the line at \$6.2 million including a \$5.0 million working capital line. Lynch Systems has a February 2002 commitment from another bank to provide a \$6 million export/ import line, a \$2 million domestic revolving credit line, and a \$944 thousand term loan. Interest rates will be variable and would currently average about 4.6 percent. All of the new lender's loan conditions have been met and the lender expects to close the loan by mid-April 2002. This new financing will be used to repay the existing Lynch Systems debt.

Cash payments for interest were \$2.0 million, \$10.4 million, and \$10.3 million for the years ended December 31, 2001, 2000 and 1999, respectively. Interest payments in 2001 are substantially below 2000 due to Spinnaker's defaulting on interest payments.

Aggregate principal maturities of long-term debt (excluding Spinnaker) for each of the next five years that total 2.1 million are as follows: 2002 — \$521 thousand; 2003 — \$816 thousand; 2004 — \$863 thousand; and 0 thereafter.

**7. Minority Interests and Related Party Transactions**

Pursuant to a subscription agreement entered into on March 11, 2000, the Company sold 100,000 shares of its Common Stock to Mario J. Gabelli, Chairman of the Company at that time and current Vice-Chairman of the Company, for \$30 per share, in cash, or \$3 million in total, which represented a premium of 14.6% above the closing price of \$26.125 per share of the stock on the American Stock Exchange on March 9, 2000, the date said sale was authorized by the Board of Directors.

The sale was exempt from registration under the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof. The proceeds were available for general corporate purposes, including possible acquisitions. The sale was ratified by the shareholders of the Company at its Annual Meeting held on May 11, 2000.

***Transactions with Certain Affiliated Persons***

Mr. Gabelli is affiliated with various entities which he directly or indirectly controls and which are engaged in various aspects of the securities business. During 2001, the Company and its subsidiaries engaged in various transactions with certain of these entities and the amount of commissions, fees, and other remunerations paid to such entities, excluding reimbursement of certain expenses related to Mr. Gabelli's employment by the Corporation, was not material.

On October 1, 2001, the Company transferred its' principal executive offices to Providence, Rhode Island from Rye, New York. These offices are shared with Avtek, Inc. ("Avtek") a private holding company co-owned by Mr. Papitto (Company Chairman) and Mr. Gabelli. Since August 2001, Avtek and the Company have shared, on an approximately equal basis, (i) all occupancy costs of the shared premises and

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

(ii) the salary expense of certain persons employed by Avtek at the premises (including Mr. McGrail, the Company's President and Chief Operating Officer and Mr. Keller, the Company's Chief Financial Officer, and other administrative and clerical personnel) whose services are provided to both the Company and Avtek. The Company's share of such occupancy and salary costs in 2001 was \$73,000, a portion of which represents compensation to Mr. McGrail and Mr. Keller that is reported in the Summary Compensation Table of the Proxy Statement which was paid subsequent to December 31, 2001.

In the opinion of management, the method of allocating these costs was reasonable; however, the costs of these services allocated to the Company are not necessarily indicative of the costs that would have been included on a stand alone basis.

***Equity Transactions***

Effective July 31, 2001, Louis A. Guzzetti, Jr. resigned from the Board of Directors of the Company. In connection with Mr. Guzzetti's resignation, on August 9, 2001, the Company purchased 12,300 shares of its Common Stock for its treasury from Mr. Guzzetti for a purchase price of \$396,204. Such purchase price was equal to the outstanding principal amount and unpaid interest on the loans made by the Company to Mr. Guzzetti on June 5, 2000 and September 20, 2000 to finance his original purchase of such Common Stock.

Mr. Gabelli's loan to the Company in the amount of \$371,000 to fund the loan to Mr. Guzzetti, which was issued in September, 2000 at an initial interest rate of 7.5% per annum adjusted prospectively on each interest payment date to two points below the prime rate, was repaid to Mr. Gabelli by the Company on August 10, 2001.

**8. Spinnaker Chapter 11 Reorganization Proceeding**

On November 13, 2001 (the "Filing Date"), Spinnaker and its Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and Entoleter, Inc. subsidiaries filed voluntary petitions for relief under chapter 11 of the United States Bankruptcy Code (11 U.S.C. & 101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the "Court"). The cases are being jointly administered under Case No. 01-38066. Effective December 28, 2001, Spinnaker's Common Stock and Class A Common Stock were delisted from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligations to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the "Letter of Intent") with WR Capital Partners, LLC ("WR Capital") whereby SP Acquisition LLC ("SP Acquisition"), and acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker's (and its subsidiaries') assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations), subject to adjustment. Entoleter's assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement ("the Asset Purchase Agreement") with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker's assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

Spinnaker's equity holders. As a result, management believes that the Company's investment in Spinnaker is worthless.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter's assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 15, 2002. If the sale closes, Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter's sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (I) and (ii), liquidate Entoleter's assets. (See Note 17).

**9. Stock Option Plans**

On December 10, 2001, the Board of Directors approved, subject to shareholder approval at the May 2002 Annual Meeting, the 2001 Equity Incentive Plan and the issuance of up to 300,000 options to purchase shares of Company common stock to certain employees of the Company, of which 228,000 options were granted (subject to shareholder approval) at \$17.50 per share on December 10, 2001. As the grants required shareholder approval, they are not considered issued until the approval is received. As a result, the Company may be required to record a non-cash charge associated with these options if the market price of the Company's stock exceeds \$17.50 at the approval date. If approved, 180,000 of these options would be fully vested, with the remaining options vesting quarterly over the next three years.

Spinnaker has two plans (Directors' and Stock Incentive Plans) under which stock options for the purchase of common shares can be granted. Total options outstanding under these plans were 82,000 and 92,000 at weighted average exercise prices of \$21.53 and \$24.95 per share at December 31, 2000 and 1999, respectively. At December 31, 2000, 44,669 options were exercisable. These options are not presented at December 31, 2001 due to the deconsolidation of Spinnaker (see Note 1).

The pro forma effect on the Company's operations, under the disclosure requirements of FAS 123 was net loss of \$3,464,000 and \$2,832,000 and basic and diluted loss per share of (\$2.32) and (\$2.00) in 2000 and 1999, respectively. The fair value of each option grant was estimated using the Black-Scholes option-pricing model, assuring 50% volatility, 6% risk-free interest rates, a 3-year expected option life and no dividends. No FAS 123 disclosure has been provided for 2001 as such amounts are not materially different from reported results.

**10. Shareholders' Equity**

The Board of Directors has authorized the purchase of up to 400,000 shares of Common Stock. Through December 31, 2000, 238,991 shares had been purchased at an average cost of \$14.88 per share.

On February 1, 1996, the Company adopted a plan to provide a portion of the compensation for its directors in common shares of the Company. The amount of common stock is based upon the market price at the end of the previous year. Through December 31, 2001, a total of 4,126 shares have been awarded under this program. No stock was issued for compensation during 2001, 2000 and 1999.

Both M-tron and Lynch Systems have plans that provided certain former shareholders with Stock Appreciation Rights (SAR's). These SAR's are fully vested and expire at the earlier of certain defined events or 2008 to 2010. These SAR's provide the participants a certain percentage, ranging from 1-5%, of the increase in the defined value of M-tron and Lynch Systems, respectively. Vested amounts are payable at the holder's option in cash or equivalent amount of M-tron or Lynch Systems stock. Expense related to the SAR's was \$195,000 in 2001, \$145,000 in 2000, and \$62,000 in 1999. At December 31, 2001 and 2000 \$402,000 and \$207,000 respectively are accrued for the SARs.

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Subsequent to the spin off of Interactive in 1999, the Company, with the concurrence of the holders of all outstanding Stock Appreciation Rights units, terminated its Stock Appreciation Rights program for corporate management, including all outstanding units, thus eliminating possible future profit and loss and cash flow distortions associated with the program. As a result of the termination, the Company recorded approximately \$700,000 of related corporate expense in the fourth quarter of 1999.

**11. Income Taxes**

The Company files consolidated federal income tax returns which include all subsidiaries including Interactive through the date of the spin off in 1999, but excluding Spinnaker for all periods.

Deferred income taxes for 2001 and 2000 are provided for the temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities. Cumulative temporary differences and carry-forwards at December 31, 2001 and 2000 are as follows:

	December 31, 2001		December 31, 2000	
	Deferred Tax Asset	Deferred Tax Liability	Deferred Tax Asset	Deferred Tax Liability
	(In Thousands)			
Inventory reserve	\$ 744	\$ —	\$ 465	\$ —
Fixed assets written up under Purchase accounting and tax over book depreciation	—	499	—	5,249
Basis difference in subsidiary and affiliate Stock	—	—	—	1,105
Net operating losses of Subsidiaries	—	—	6,027	—
Other reserves and accruals	1,215	—	4,268	—
Other	—	1,050	—	398
Capital loss and other carry forwards	938	—	—	—
Total deferred income taxes	2,897	1,549	10,760	\$6,752
Valuation allowance	(938)	—	(3,136)	—
	\$1,959	—	\$ 7,624	—

At December 31, 2001, Lynch Corporation had capital loss carry-forwards that are fully offset by a valuation allowance of \$938,000. At December 31, 2000, Spinnaker had federal and state net operating loss carry-forwards. For financial reporting purposes, a valuation allowance of \$3.1 million was recognized to offset the deferred tax assets related to those carry-forwards.

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The provision (benefit) for income taxes from continuing operations is summarized as follows:

	2001	2000	1999
	(In Thousands)		
Current:			
Federal	\$(439)	\$ 136	\$ (158)
State and local	274	—	—
Foreign	22	—	—
Total Current	(143)	136	(158)
Deferred:			
Federal	489	(2,731)	(2,386)
State and local	12	(198)	—
Total Deferred	501	(2,929)	(2,386)
	\$ 358	\$(2,793)	\$(2,544)

A reconciliation of the provision (benefit) for income taxes from continuing operations and the amount computed by applying the statutory federal income tax rate to income before income taxes, minority interest and extraordinary item:

	2001	2000	1999
	(In Thousands)		
Tax (benefit) at statutory rate	\$ (9,043)	\$(6,028)	\$(3,211)
State and local taxes, net of federal benefit	189	(130)	—
Amortization of goodwill	—	111	60
Operating losses of subsidiaries	—	—	164
Provision for contingencies	—	—	338
Spinnaker operating loss	18,533	—	—
Deconsolidation gain	(10,132)	—	—
Foreign Sales Corporation	(236)	(199)	—
Valuation allowance	938	3,136	—
Other	109	317	105
	\$ 358	\$(2,793)	\$(2,544)

Gain (loss) before income taxes from foreign operations was \$671,000, (\$313,000) and (\$579,000) in 2001, 2000, and 1999 respectively.

Income tax payments were \$1.2 million, \$1.3 million, and \$1.2 million for the years 2001, 2000 and 1999, respectively.

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**12. Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss, net of related tax, at December 31, 2001, 2000, and 1999 are as follows:

	2001	2000	1999
	(In Thousands)		
Balance beginning of year	\$(71)	\$(40)	\$ 59
Foreign currency translation	69	(31)	(40)
Distribution to Lynch Interactive Corporation	—	—	(59)
Accumulated other comprehensive loss	\$ (2)	\$(71)	\$(40)

**13. Employee Benefit Plans**

The Company, through its operating subsidiaries, has several and various employee retirement type plans including defined benefit, defined contribution, multi-employer, profit sharing, and 401 (k) plans. The following table sets forth the consolidated expenses (including Spinnaker's expenses through September 30, 2001) for these plans:

	2001	2000	1999
	(In Thousands)		
Defined contribution:			
Lynch Systems & M-tron	\$ 17	\$ 38	\$ 19
Spinnaker	346	335	542
Defined benefit (Spinnaker)	202	98	166
Multi-employer (Spinnaker)	42	88	121
Total	\$607	\$559	\$848

Under the Lynch Systems and M-tron defined contribution plan, the Company contributes up to a maximum of 25 percent of participants contributions that do not exceed \$800 per participant in the plan year. The Company contribution occurs at the end of the plan year and the participant is immediately vested in the employers' contribution.

Spinnaker and its subsidiaries have several defined benefit plans (both Union and non-Union). At December 31, 2000, total benefit obligations for these plans were \$2.4 million. The assumptions used in determining the obligations included average discount rates of 8.0%, an average compensation increases of 0 to 4% and average long-term rate of return on plan assets of 8%. Total plan assets were \$2.0 million at December 31, 2000. Spinnaker also has a defined contribution plan for substantially all employees, under which Spinnaker can match up to 50% of employee contributions not exceeding 8% of compensation. No disclosure was made for 2001 due to the deconsolidation of Spinnaker (see Note 1).

**14. Commitments and Contingencies**

In the normal course of business, subsidiaries of the Company are defendants in certain product liability, worker claims and other litigation in which the amounts being sought may exceed insurance coverage levels. The resolution of these matters is not expected to have a material effect on the Company's financial condition or operations.

The Company, Lynch Interactive Corporation ("Interactive"), and several other parties have been named as defendants in a lawsuit brought under the so-called "qui tam" provisions of the federal False Claims Act in the United States District Court for the District of Columbia. Although the complaint was filed under



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**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

seal with the court on February 14, 2001, and the seal was lifted on January 11, 2002, the defendants have yet to be formally served with the complaint. The main allegation in the case is that the defendants participated in the creation of “sham” bidding entities that allegedly defrauded the federal Treasury by improperly participating in certain Federal Communications Commission spectrum auctions restricted to small businesses, as well as obtaining bidding credits in other spectrum auctions allocated to “small” and “very small” businesses. The lawsuit seeks to recover an unspecified amount of damages, which would be subject to mandatory trebling under the statute.

The U.S. Department of Justice has notified the court that it has declined to intervene in the case. The defendants strongly believe that this lawsuit is completely without merit and intend to defend the suit vigorously. Furthermore, the Company believes that, under the separation agreement between the Company and Interactive pursuant to which Interactive was spun-off to the Company’s shareholders on September 1, 1999, Interactive would be obligated to indemnify the Company for any losses or damages incurred by the Company as a result of this lawsuit.

Rent expense under operating leases was \$846,000 (including Spinnaker for nine months), \$1,213,000, and \$1,222,000 for the years ended December 31, 2001, 2000 and 1999, respectively. The Company leases certain property and equipment, including warehousing and sales and distribution equipment, under operating leases that extend from one to five years. Certain of these leases have renewal options and escalation provisions.

Future minimum rental payments under long-term non-cancelable operating leases for the five years subsequent to December 31, 2001 are as follows (in thousands):

2002	\$303
2003	167
2004	156
2005	108
2006	52
Thereafter	0
	<hr/>
	\$786
	<hr/>

**15. Segment Information**

The Company has four reportable business segments. The largest is Spinnaker Coating’s adhesive backed label stock for labels and related applications. The second largest segment is Lynch Systems glass manufacturing equipment business. Frequency control devices (quartz crystals and oscillators) manufactured and sold by M-tron is the third segment. Entoleter (subsidiary of Spinnaker Industries, Inc.) manufactures and sells industrial process equipment and is the fourth segment. Spinnaker Coating and Entoleter results for 2001 represent the nine-month period ending September 30, 2001 pursuant to the “deconsolidation” of Spinnaker on September 30, 2001 (see Note 1). Each of the businesses is located domestically and consolidated export sales (primarily Canada and China) were approximately \$38.3 million in 2001, \$54.7 million in 2000, and \$31.5 million in 1999. For the year ended December 31, 2001, one customer accounted for \$5.6 million or 24.5 percent of Lynch Systems’ sales while one customer represented \$2.9 million or 13.5% of frequency control sales. The Company considers concentrations of credit risk to be minimal due to its diverse customer base and because it requires letters of credit of most foreign customers to support a significant portion of the purchase price.

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

M-tron attempts to utilize standard parts and components that are available from multiple vendors located in the United States or internationally; however, some components used in its products are available from only a limited number of sources.

EBITDA (before corporate allocation) for operating segments is equal to operating profit before depreciation, amortization and allocated corporate expenses. EBITDA is presented because it is a widely accepted financial indicator of value and ability to incur and service debt. EBITDA is not a substitute for operating income or cash flows from operating activities in accordance with generally accepted accounting principles.

Operating profit (loss) is equal to revenues less operating expenses, excluding unallocated general corporate expenses, interest and income taxes. The Company allocates a portion of its general corporate expenses to its operating segments. Such allocation was \$289,000 in 2001 and \$300,000 per year in 2000 and 1999. Identifiable assets of each industry segment are the assets used by the segment in its operations excluding general corporate assets. General corporate assets are principally cash and cash equivalents, short-term investments and certain other investments and receivables.

	Years ended December 31		
	2001	2000	1999
<b>Revenues</b>			
Adhesive-backed label stock	\$ 90,163	\$150,136	\$155,112
Glass manufacturing equipment	26,047	23,608	5,656
Frequency control devices	21,593	39,855	26,484
Industrial process equipment	3,270	5,597	6,970
Consolidated total	<u>\$141,073</u>	<u>\$219,196</u>	<u>\$194,222</u>
<b>EBITDA (before corporation allocation)</b>			
Adhesive-backed label stock	\$ (4,755)	\$ 99	\$ 8,940
Glass manufacturing equipment	5,125	3,239	(1,766)
Frequency control devices	(1,770)	4,054	2,540
Industrial process equipment	77	440	473
Corporate manufacturing expenses	(1,140)	(1,973)	(1,930)
Total manufacturing	<u>(2,463)</u>	<u>5,859</u>	<u>8,257</u>
Corporate expenses, net	(985)	(1,451)	(1,152)
Restructuring charge — Spinnaker	(1,520)	(1,650)	—
Consolidated total	<u>\$ (4,968)</u>	<u>\$ 2,758</u>	<u>\$ 7,105</u>

LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	Years ended December 31		
	2001	2000	1999
<b>Operating Profit</b>			
Adhesive-backed label stock	\$ (7,860)	\$ (5,137)	\$ 4,155
Glass manufacturing equipment	4,778	2,867	(2,042)
Frequency control devices	(2,549)	3,345	1,900
Industrial process equipment	(22)	280	321
Corporate manufacturing expenses	(1,065)	(1,873)	(2,794)
Total manufacturing	(6,718)	(518)	1,540
Unallocated Corporate expense	(1,656)	(1,751)	(1,455)
Gain on deconsolidation	27,406	—	—
Restructuring charge — Spinnaker	(38,272)	(2,708)	—
Consolidated Total	\$ (19,240)	\$ (4,977)	\$ 85
<b>Depreciation and Amortization</b>			
Adhesive-backed label stock	\$ 3,105	\$ 5,236	\$ 4,785
Glass manufacturing equipment	461	472	376
Frequency control devices	879	809	740
Industrial process equipment	99	160	152
Corporate manufacturing expenses	15	1,058	181
Consolidated Total	\$ 4,559	\$ 7,735	\$ 6,234
<b>Capital expenditures</b>			
Adhesive-backed label stock	\$ 430	\$ 2,631	\$ 2,625
Glass manufacturing equipment	217	183	154
Frequency control devices	429	1,476	804
Industrial process equipment	28	33	212
Consolidated Total	\$ 1,104	\$ 4,323	\$ 3,795
<b>Total Assets</b>			
Adhesive-backed label stock	\$ —	\$116,746	\$105,674
Glass manufacturing equipment	22,496	17,908	7,695
Frequency control devices	7,901	18,210	10,940
Industrial process equipment	—	2,285	2,730
General Corporate	1,448	7,671	84,153
Consolidated Total	\$ 31,845	\$162,820	\$211,192
Total operating profit for reportable segments			
Other profit or loss:	\$ (19,240)	\$ (4,977)	\$ 85
Investment income	384	1,481	2,354
Interest expense	(7,741)	(11,432)	(11,882)
Impairment of Spinnaker's investment in warrants	—	(2,800)	—
Income (loss) from continuing operations before income taxes, minority interests and extraordinary items	\$ (26,597)	\$ (17,728)	\$ (9,443)

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LYNCH CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting (see Note 1).

**16. Quarterly Results of Operations (unaudited)**

The following is a summary of the quarterly results of operations for the years ended December 31, 2001 and December 31, 2000 (in thousands, except per share amounts):

	2001 Three Months Ended			
	Mar. 31	June 30	Sep. 30(b)	Dec. 31(b)
Sales and revenues	\$ 53,548	\$45,353	\$31,982	\$10,190
Gross profit	4,995	692	2,661	2,435
Operating profit (loss)(a)	(37,093)	(5,870)	24,379	(656)
Net income (loss)	(36,070)	(8,673)	23,082	(1,277)
Basic and diluted earnings (loss) per share	(23.89)	(5.74)	15.36	(0.85)

  

	2000 Three Months Ended			
	Mar. 31(c)	June 30(c)	Sep. 30	Dec. 31(d)
Sales and revenues	\$52,474	\$53,008	\$56,192	\$57,522
Gross profit	6,147	7,560	8,266	4,243
Operating profit (loss)	(142)	1,532	508	(6,875)
Income (loss) from continuing operations before extraordinary item	(758)	140	226	(5,291)
Net income (loss)	496	1,131	226	(5,291)
Basic and diluted earnings (loss) per share:				
Income (loss) from continuing operations before extraordinary item	(.53)	0.09	0.15	(3.50)
Net income (loss)	.35	0.75	0.15	(3.50)

NOTE:

- a) Includes restructuring costs applicable to Spinnaker of: 1st Quarter — \$36,484; 2nd Quarter — \$5,051; 3rd Quarter — \$219 and gain on deconsolidation of \$27,406 in the 3rd Quarter.
- b) Effective September 30, 2001, the Company deconsolidated Spinnaker (see Note 1). As a result, fourth quarter results do not include Spinnaker results.
- c) Includes gain on early extinguishments of debt of \$2.2 million after income taxes and minority interests.
- d) Includes restructuring charge of approximately \$2.2 million, deferred tax asset valuation allowance of \$3.1 million and investment write-down of \$2.8 million all at Spinnaker.

**17. Subsequent Events**

On March 28, 2002, Spinnaker Industries (excluding Entoleter) was acquired by S P Acquisition LLC (an entity of WR Capital Partners LLC) for \$25.8 million. On March 26, 2002, an auction was held with a subsequent hearing on March 28, 2002 for the Bankruptcy Court which approved the sale of Entoleter to Welton, LLC for approximately \$0.9 million plus certain assumed obligations.

**LYNCH CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

In each case, no return to equity holders is anticipated. Therefore, as a result, the Company anticipates eliminating its remaining interest in Spinnaker and its subsidiaries upon conclusion of the bankruptcy proceedings expected to occur in the second quarter of 2002. At that time, the \$19,420,000 “loss in excess of investment” on the Company’s December 31, 2001 balance sheet will become a non-cash income item and increase shareholders’ equity. If this event would have occurred on December 31, 2001, the Company’s pro-forma equity would have been \$11,969,000, not the reported deficit amount of (\$7,451,000).

**SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF  
REGISTRANT LYNCH CORPORATION**

**CONDENSED BALANCE SHEET**

	2001	2000
(In Thousands)		
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and Cash Equivalents	\$ 2,208	\$ 1,928
Dividend Receivable From Subsidiary	—	1,500
Deferred Income Taxes	412	412
Other Current Assets	76	980
	2,696	4,820
OFFICE EQUIPMENT (Net of depreciation)	—	16
OTHER ASSETS (principally investment in and amounts due from wholly owned subsidiaries)	10,517	13,057
	13,213	17,893
<b>TOTAL ASSETS</b>	<b>\$13,213</b>	<b>\$17,893</b>
<b>LIABILITIES AND SHAREHOLDERS' (DEFICIENCY) EQUITY</b>		
CURRENT LIABILITIES	\$ 1,213	\$ 2,303
LONG TERM LIABILITIES	31	158
LOSS IN EXCESS OF INVESTMENT	19,420	—
TOTAL SHAREHOLDERS' (DEFICIENCY) EQUITY	(7,451)	15,432
	13,213	17,893
<b>Total Liabilities and Shareholders' (Deficiency) Equity</b>	<b>\$13,213</b>	<b>\$17,893</b>

\* On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

**LYNCH CORPORATION**  
**CONDENSED FINANCIAL INFORMATION OF REGISTRANT**  
**CONDENSED STATEMENT OF OPERATIONS**

	Year Ended December 31		
	2001	2000	1999
	(In Thousands)		
Interest, Dividends & Gains on Sale of Marketable Securities	\$ 209	\$ 187	\$ 17
Dividend from Subsidiary	—	1,500	—
Interest & Other Income from Subsidiaries	24	348	23
<b>TOTAL INCOME</b>	<b>\$ 233</b>	<b>\$ 2,035</b>	<b>40</b>
Costs & Expenses:			
Unallocated Corporate Administrative Expense	1,001	1,451	1,155
Interest Expense	23	15	7
Interest Expense to Subsidiaries	—	—	23
<b>TOTAL COST AND EXPENSE</b>	<b>1,024</b>	<b>1,466</b>	<b>1,185</b>
<b>INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY IN NET</b>			
LOSS OF SUBSIDIARIES	(791)	569	(1,145)
Income Tax Benefit (Provision)	269	(215)	321
Equity in Net Loss of Subsidiaries	(22,416)	(3,792)	(759)
<b>NET LOSS</b>	<b>\$(22,938)</b>	<b>\$(3,438)</b>	<b>\$(1,583)</b>

\* On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

**LYNCH CORPORATION**  
**CONDENSED FINANCIAL INFORMATION OF REGISTRANT**  
**CONDENSED STATEMENTS OF CASH FLOW**

	Year Ended December 31		
	2001	2000	1999
	(In Thousands)		
Cash provided from (used in) Operating Activities	\$(1,220)	\$(2,210)	\$ 405
INVESTING ACTIVITIES:			
Investment in Lynch Manufacturing	—	—	981
Dividend from subsidiaries	1,500	—	—
<b>NET CASH PROVIDED FROM INVESTING ACTIVITIES</b>	<b>1,500</b>	<b>—</b>	<b>981</b>
FINANCING ACTIVITIES:			
(Purchase) Sale of Treasury Stock	—	1,191	(523)
Issuance of Common Stock	—	1,809	—
Other	—	(16)	—
<b>NET CASH (USED IN) PROVIDED FROM FINANCING ACTIVITIES</b>	<b>—</b>	<b>2,984</b>	<b>(523)</b>
<b>TOTAL INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>280</b>	<b>774</b>	<b>863</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>1,928</b>	<b>1,154</b>	<b>291</b>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 2,208</b>	<b>\$ 1,928</b>	<b>\$1,154</b>

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**NOTE A — BASIS OF PRESENTATION**

In the parent company's financial statements, the Company's investment in subsidiaries is stated at cost plus equity in undistributed earnings of the subsidiaries.

**NOTE B — SPIN OFF OF LYNCH INTERACTIVE CORPORATION**

On August 12, 1999, the Board of Directors approved a plan to distribute the stock of Lynch Interactive Corporation on a one for one basis to the shareholders of Lynch Corporation ("spin off"). Lynch completed the spin off of Lynch Interactive Corporation ("Interactive") on September 1, 1999, to stockholders of record on August 23, 1999. Pursuant to the spin off, each Lynch shareholder received one share of Interactive common stock for each share of Lynch owned. Lynch had received a private letter ruling from the Internal Revenue Service that the spin off would be tax free to Lynch shareholders. Interactive is listed on the American Stock Exchange under the symbol "LIC".

**NOTE C — DIVIDENDS FROM SUBSIDIARIES**

Dividends paid to Lynch Corporation from the Registrant's consolidated subsidiaries were \$1,500,000 in 2001. No dividends were paid in 2000 and 1999 and no other dividends were received from subsidiaries or investees.



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**NOTE D — SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR ADDITIONAL INFORMATION.**

**LYNCH CORPORATION AND SUBSIDIARIES**

**SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS  
YEARS ENDED DECEMBER 31, 2001, 2000 AND 1999**

Column A	Column B	Column C		Column D	Column E
Description	Balance at Beginning of Period	Additions		Deductions(B)	Balance at End of Period
		Charged to Costs and Expenses	Charged to Other Accounts(A)		
Year ended December 31, 2001					
Allowance for uncollectible	\$1,582,000	\$ 120,000	\$(589,000)	\$995,000	\$ 118,000
Year ended December 31, 2000					
Allowance for uncollectible	\$ 361,000	\$1,312,000	\$ 0	\$ 91,000	\$1,582,000
Year ended December 31, 1999					
Allowance for uncollectible	\$ 395,000	\$ 81,000	\$ 0	\$115,000	\$ 361,000

(A) Impact of the deconsolidation of Spinnaker Industries, Inc. on September 30, 2001 (as discussed in Note 1 to the Consolidated Financial Statements included elsewhere herein).

(B) Uncollectible accounts written off are net of recoveries (majority attributable to Spinnaker in 2001).

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Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LYNCH CORPORATION

BY: /s/ RALPH R. PAPITTO

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RALPH R. PAPITTO  
*Chief Executive Officer*  
*(Principal Executive Officer)*

March 31, 2002

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Capacity</u>	<u>Date</u>
<u>/s/ MARIO J. GABELLI</u> MARIO J. GABELLI	Vice Chairman of the Board of Directors and Director	March 31, 2002
<u>/s/ RALPH R. PAPITTO</u> RALPH R. PAPITTO	Principal Executive Officer, Chairman of the Board of Directors and Director	March 31, 2002
<u>/s/ E. VAL CERUTTI</u> E. VAL CERUTTI	Director	March 31, 2002
<u>/s/ AVRUM GRAY</u> AVRUM GRAY	Director	March 31, 2002
<u>/s/ RICHARD E. MCGRAIL</u> RICHARD E. MCGRAIL	President, Chief Operating Officer and Director	March 31, 2002
<u>/s/ RAYMOND H. KELLER</u> RAYMOND H. KELLER	Principal Financial and Accounting Officer and Director	March 31, 2002

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### EXHIBIT INDEX

Exhibit No.	Description
2	(a) Asset Purchase Agreement (“Asset Purchase Agreement”) dated January 18, 2002 by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and SP Acquisition, LLC.††
	(b) Asset Purchase Agreement Amendment No. 1 dated February 15, 2002.††
	(c) Asset Purchase Agreement Amendment No. 2 dated February 25, 2002.††
	(d) Asset Purchase Agreement Amendment No. 3 dated March 5, 2002.††
	(e) Asset Purchase Agreement Amendment No. 4 dated March 8, 2002.††
	(f) Asset Purchase Agreement Amendment No. 5 dated March 18, 2002.††
	(g) Schedules to Asset Purchase Agreement dated January 18, 2002.††
	(h) United States Bankruptcy Court Order dated March 6, 2002; In Re: Spinnaker Industries, Inc., et al., C.A. No. 01-38066.††
3	(a) Restated Articles of Incorporation of Registrant (incorporated by reference to Exhibit 3(a) of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 1987).
	(b) By-laws of the Registrant, (incorporated by reference to the Exhibit 3(b) of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 1987).
4	(a) Purchase Agreement, dated October 18, 1996 (the “Purchase Agreement”) among Spinnaker Industries, Inc., a Delaware corporation (“Spinnaker”), Brown-Bridge Industries, Inc., a Delaware corporation (“Brown-Bridge”), Central Products Company, a Delaware corporation (“Central Products”), and Entoleter, Inc., (“Entoleter”) and together with Brown-Bridge and Central Products, (the “Guarantors”) and BT Securities Corporation (the “Initial Purchaser”) (incorporated by reference to Exhibit 4.1 to Registrant’s Form 8-K, dated October 23, 1996).
	(b) Indenture, dated October 23, 1996, among Spinnaker, the Guarantors and the Chase Manhattan Bank, as Trustee (incorporated by reference to Exhibit 4.3 to Registrant’s Form 8-K, dated April 19, 1996).
	(b)(i) First Supplemental Indenture dated as of March 17, 1998, among Spinnaker Industries, Inc., Central Products Company, Entoleter, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and the Chase Manhattan Bank, as Trustee (incorporated by reference by Exhibit 99.6 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998.)
	(c) Credit Agreement (the “Spinnaker Credit Agreement”) amended as of December 31, 1997, among Central Products Company, Brown-Bridge Industries, Inc. and Entoleter, Inc. as Borrowers, Spinnaker Industries, Inc. as Guarantor, each of the financial institutions listed on Schedule 1 thereto, BT Commercial Corporation, as Agent, Transamerican Business Credit Corporation, as Collateral Agent, and Bankers Trust Company as Issuing Bank (incorporated by reference to Exhibit 99.1 to Registrant’s Form 8-K dated October 23, 1996).
	(c)(i) Fourth Amendment to the Spinnaker Credit Agreement (incorporated by reference to Exhibit 9.3 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
	(c)(ii) Fifth Amendment to Spinnaker Credit Agreement (incorporated by reference to Exhibit 9.4 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
	(c)(iii) Sixth Amendment to the Spinnaker Credit Agreement (incorporated by reference by Exhibit 9.5 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
	(d) Refinanced Credit Agreement among Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and Entoleter, Inc. as Borrowers, Spinnaker Industries, Inc. as Guarantor, each of the financial institutions listed as Schedule 1 hereto and Transamerica Business Corporation, as Agent, dated August 9, 1999 and the First, Second and Third Amendments thereto (incorporated by reference to Exhibits 10.5, 10.6, 10.7 and 10.8 to Spinnaker’s Form 10-K for the year ended December 31, 1999).

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Exhibit No.	Description
(d)(i)	Fourth Amendment to financed Credit Agreement dated April 17, 2000 (incorporated by reference to Exhibit 10.1 to Spinnaker's Form 10-Q for the quarter ended March 31, 2000).
(d)(ii)	Fifth Amendment to Refinanced Credit Agreement dated September 30, 2000 (incorporated by reference to Exhibit 10.1 to Spinnaker's Form 10-Q for the quarter ended September 30, 2000).
(d)(iv)	Sixth Amendment to Refinanced Credit Agreement dated March 2001 (incorporated by reference to Exhibit 10.16 to Spinnaker's Form 10-K for the year ended December 31, 2001).

The Registrant, by signing this Form 10-K Annual Report, agrees to furnish to the Securities and Exchange Commission a copy of any long-term debt instrument where the amount of the securities authorized thereunder does not exceed 10 percent of the total assets of the Registrant on a consolidated basis.

10	(a)*	Lynch Corporation 401(k) Savings Plan.
	(b)	Acquisition Agreement between Brown-Bridge Acquisition Corporation and Kimberly-Clark Corporation, dated June 15, 1994 (exhibit omitted) (incorporated by reference to Exhibit 10@ to Registrant's Form 10-Q for the quarter ended June 10, 1994).†
	(c)*	Management Agreement, dated as of June 10, 1994, by and among Boyle, Fleming, George & Co., Inc. and Safety Railway Service Corporation (incorporated by reference by Exhibit 7.1 to the Registrant's Form 8-K, dated June 13, 1994).
	(d)	Subscription Agreement dated March 9, 2000 between Registrant and Mario J. Gabelli (incorporated by reference to Exhibit E to Amendment No. 41 to Schedule 13D of Registrant dated March 15, 2000 filed by Mario J. Gabelli et. al.).
	(e)	Warrant Purchase Agreement dated as of June 10, 1994, by and among Boyle, Fleming, George & Co., Inc. and Safety Railway Service Corporation (incorporated by reference by Exhibit 7.1 to the Registrant's Form 8-K, dated June 13, 1994).
	(f)	A Warrant, dated as of June 10, 1994, executed by Safety Railway Service Corporation (incorporated by reference to Exhibit 7.1 to Registrant's Form 8-K, dated June 12, 1994).
	(g)	Asset Purchase Agreement, dated as of June 15, 1994, between Kimberly-Clark Corporation and Brown-Bridge Acquisition Corp. (Exhibits omitted) (incorporated by reference to Exhibit 10@ to Registrant's Form 10-Q for the quarter ended June 30, 1994).†
	(h)	Stock Purchase and Loan Program (incorporated by reference to Exhibit 10(p) to Registrant's Form 10-K for the year ended December 31, 1994).
	(i)	Shareholders' and Voting Agreement, dated September 16, 1994, among Safety Railway Service Corporation, Brown-Bridge Industries, Inc. and the other stockholders of Brown-Bridge (incorporated by reference to Exhibit 10(q) to Registrant's Form 10-K for the year ended December 31, 1994).
	(j)	Put Option Agreement, dated September 16, 1994, among Safety Railway Service Corporation, Brown-Bridge Industries, Inc. and certain stockholders of Brown-Bridge (incorporated by reference to Exhibit 10 (q) to Registrant's Form 10-K for the year ended December 31, 1994).
	(k)*	Directors Stock Plan (incorporated by reference to Exhibit 10(o) to Registrant's Form 10-K for the year ended December 31, 1997).
	(l)	Amended Phantom Stock Plan (incorporated by reference to Exhibit 10(p) to Registrant's Form 10-Q for the year ended September 30, 1998).
	(m)	Stock and Asset Purchase Agreement, dated as of September 27, 1995, by and among Central Products Acquisition Corp. Unisource Worldwide, Inc. and Alco Standard Corporation (incorporated by reference to Exhibit 7.1 to Registrant's Form 8-K, dated October 19, 1995).†
	(n)	Agreement and Plan of Merger (Brown-Bridge Minority Interest), by and among Spinnaker Industries, Inc., BB Merger Corp., Brown-Bridge Industries, Inc. and the stockholder of Brown-Bridge Industries, Inc. on Exhibit A thereto (incorporated by reference to Exhibit 99.2 to Registrant's Form 8-K, dated April 19, 1996).†
	(o)	Lease Agreement between Registrant and Gabelli Funds, Inc. (incorporated by reference to Exhibit 10(a) (a) to Registrant's Form 10-Q for the Quarter Ended March 31, 1998).

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Exhibit No.	Description
(p)	Asset Purchase Agreement, dated as of November 18, 1997, by and between S.D. Warren Company (“Seller”) and Spinnaker Industries, Inc. (incorporated by reference to Exhibit 2.1 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).
(p)(i)	First Amendment to Asset Purchase Agreement, dated March 17, 1998, by and between S. D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 4.2 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).†
(p)(ii)	Subordinated Note, dated March 17, 1998, issued by Spinnaker Industries, Inc. to S.D. Warren Company in the original principal amount of \$7 million bearing interest at a rate of 20% per annum (incorporated by reference to Exhibit 4.1 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).
(p)(iii)	Site Separation and Service Agreement, dated March 17, 1998, between S.D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 99.1 to the Form 8-K of Spinnaker Industries, Inc., dated March 17, 1998).
(p)(iv)	Lease Agreement, dated March 17, 1998, between S.D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 99.2 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998.)
(q)	Stock Purchase Agreement between Spinnaker Industries, Inc. and Intertape Polymer Group, Inc., dated April 9, 2000 (incorporated by reference to Exhibit 2.1 to Spinnaker Industries, Inc. Form 8-K, dated August 16, 2000).
(r)	Asset Purchase Agreement by and among Registrant, Spinnaker Electrical Tape Company and Intertape Polymer Group, Inc., dated April 9, 2000 (incorporated by reference to Exhibit 2.2 to Spinnaker Industries, Inc. Form 8-K, dated August 16, 2000).
(s)	Information Statement of Lynch Interactive Corporation’s (incorporated by reference to Exhibit 99.1 to Lynch Interactive Corporation’s Form 10-A-1, dated August 18, 2000).
(t)	Separation Agreement, dated as of August 31, 2000, between Registrant and Lynch Interactive Corporation (incorporated by reference to Exhibit 2 to Lynch Interactive Corporation’s Form 10a-1, dated August 18, 2000).
(u)*	Letter of Understanding between Registrant and Louis A. Guzzetti (incorporated by reference to Exhibit (u) to Registrant’s Form 10-K for the year ended December 31, 1999).
(v)	Note from Louis A. Guzzetti, Jr. to Registrant (incorporated by reference to Exhibit 10(v) to Registrant’s Form 10-K for the year ended December 31, 2000).
(w)*	Agreement among Registrant, Mario J. Gabelli and Ralph R. Papitto dated August 17, 2001 pursuant to which, among other things, Registrant agreed to grant Mr. Papitto an option (incorporated by reference to Exhibit 10(w) to Registrant’s Form 8-K dated August 17, 2001).
(x)*	Amendment dated February 7, 2002 among Registrant, Mario J. Gabelli and Ralph R. Papitto, amending the Agreement at Exhibit 10(w) to terminate Registrant’s obligation to grant an option to Mr. Papitto.††
(y)*	Lynch Corporation 2001 Equity Incentive Plan adopted December 10, 2001.††
16	Letter Re: Change in Certifying Accountant (incorporated by reference to Exhibit 16 to Registrant’s Form 8-K, dated March 19, 1996).
21	Subsidiaries of the Registrant.††
23	Consent of Ernst & Young LLP.††
24	Powers of Attorney.††

\* Management contract or compensatory arrangement.

† Registrant agrees to furnish a supplemental copy of any omitted schedule to the Securities and Exchange Commission upon request.

†† Filed herewith.

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The Exhibits listed above have been filed separately with the Securities and Exchange Commission in conjunction with this Annual Report on Form 10-K or have been incorporated by reference into this Annual Report on Form 10-K. Lynch Corporation will furnish to each of its shareholders a copy of any such Exhibit for a fee equal to Lynch Corporation's cost in furnishing such Exhibit. Requests should be addressed to the Office of the Secretary, Lynch Corporation, 50 Kennedy Plaza, Suite 1250, Providence, RI 02903.

<DOCUMENT>  
<TYPE> EX-2.(A)  
<FILENAME> b421241cex2-a.txt  
<DESCRIPTION> Ex-2.(a) Asset Purchase Agreement  
<TEXT>

ASSET PURCHASE AGREEMENT

by and among

SPINNAKER INDUSTRIES, INC.,

SPINNAKER COATING, INC.,

SPINNAKER COATING-MAINE, INC.

and

SP ACQUISITION, LLC

Dated as of January 18, 2002



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SCHEDULES AND EXHIBITS

Exhibits

- A Motion of Debtors for Order Pursuant to Sections 105, 363, 365 and 1146 of the Bankruptcy Code
- B Escrow Agreement
- C Post-Closing Escrow Agreement

Schedules

- 1(f) Transamerica Encumbrances
- 2(a) (i) Permitted Encumbrances
- 2(a) (xviii) Description of Other Acquired Assets
- 3(c) Allocation of Purchase Price
- 3(d) (i) Target Statement of Net Working Capital
  
- 4(b) (ii) Assumed Prepetition Liabilities Related to Customer Claims and Rebates, Taxes and Employee Benefits to the Extent Approved by the Court and Not Satisfied Before Closing
- 4(b) (iv) Additional Pre-Petition Liabilities
- 7(b) Conflicts/Consents: Sellers
- 7(d) Executory Contracts; Assigned Contracts
- 7(e) (i) Audited Financials
- 7(e) (ii) Current Balance Sheet
- 7(f) Equipment
- 7(h) Intellectual Property
- 7(i) Compliance with Laws
- 7(k) Permits
- 7(l) Environmental Matters
- 7(m) Employee Matters
- 7(n) Absence of Certain Changes
- 7(o) Liabilities
- 7(p) Insurance
- 7(q) Taxes
- 7(t) Warranty Obligations, Pricing and Other Accommodations
- 7(u) Real Property
- 7(v) Litigation
- 8(b) Conflicts/Consents: Buyer

ASSET PURCHASE AGREEMENT

AGREEMENT, dated as of January 18, 2002, by and among SPINNAKER INDUSTRIES, INC., a Delaware corporation ("SII"), SPINNAKER COATING, INC., a Delaware corporation and wholly-owned subsidiary of SII ("SCI"), SPINNAKER COATING-MAINE, INC., a Delaware corporation and wholly-owned subsidiary of SCI ("SCMI") (SII, SCI and SCMI are sometimes individually referred to herein as "Seller" and collectively as "Sellers"), and SP ACQUISITION, LLC, a Delaware limited liability company (and, except as otherwise provided herein, any assignee to whom Buyer's rights and obligations are transferred pursuant to Section 16(i), "Buyer").

W I T N E S S E T H:

WHEREAS, SCI is engaged in the business of manufacturing and selling pressure sensitive adhesive roll and sheet products (as conducted by SCI, the "Business");

WHEREAS, on November 13, 2001, each Seller (along with Entoleter Inc., a wholly-owned subsidiary of SII) filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code (as defined below) with the United States Bankruptcy Court for the Southern District of Ohio (the "Bankruptcy Court") (collectively, the "Petition"), which petitions were procedurally consolidated for joint administration pursuant to order of the Bankruptcy Court dated November 14, 2001, commencing a case titled In re SPINNAKER INDUSTRIES, INC., et. al., Case No. 01-38066; and

WHEREAS, Sellers desire to sell to Buyer substantially all of the assets used in the Business and to assign to Buyer certain executory contracts and unexpired leases relating to the Business, and Buyer desires to purchase from Sellers such assets and assume such contracts and unexpired leases (as hereinafter defined) upon the terms and subject to the conditions of this Agreement.

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants set forth herein, the parties agree as follows:

1. DEFINITIONS

For all purposes of this Agreement, except as otherwise expressly provided herein,

(a) the terms defined in this Section 1 include the plural as well as the singular,

(b) all accounting terms not otherwise defined herein have the meanings assigned to them under GAAP (as defined below),

(c) pronouns of either gender or neuter shall include, as appropriate, the other pronoun forms,

(d) the words "herein," "hereof" and "hereunder" and other words of similar import refer to this Agreement as a whole and not to any particular Section, Paragraph or other subdivision, and

(e) the words "include," "including" and other words of similar import mean "include, without limitation" or "including, without limitation," regardless of whether any reference to "without limitation" or words of similar import is made.

(f) As used in this Agreement, the following definitions shall apply:

"Accountant" shall have the meaning assigned to that term in Section 3(d)(ii).

"Accounts Receivable" has the meaning assigned to that term in Section 2(a)(i).

"Acquired Assets" has the meaning assigned to that term in Section 2(a).

"Action" has the meaning assigned to that term in Section 14(e).

"Agreement" means this Asset Purchase Agreement, including all exhibits and schedules hereto, as the same may be amended or supplemented from time to time in accordance with its terms.

"Alternative Transaction" has the meaning assigned to that term in Section 12(b).

"Assigned Contracts" means those Contracts which Buyer desires to assume and to have Sellers assign to it which are designated as "Assigned Contracts" on SCHEDULE 7(d) (or identified in a separate schedule provided by Buyer to Sellers at least 1 Business Day prior to the Due Diligence Termination Date as Contracts to be included as Assigned Contracts). Assigned Contracts shall not include Contracts identified in a separate schedule provided by Buyer to Sellers at least 7 days before the Auction Date as Contracts to be excluded from the Assigned Contracts list in SCHEDULE 7(d) notwithstanding their initial inclusion.

"Assumed Obligations" has the meaning assigned to that term in Section 4(b).

"Auction" shall mean an auction under Section 363 of the Bankruptcy Code scheduled by the Bankruptcy Court pursuant to the Procedures Order.

"Auction Date" shall mean the date of the Auction scheduled pursuant to the Procedures Order.

"Audited Financials" has the meaning assigned to that term in Section 7(e).

"Bankruptcy Code" means title 11 of the United States Code, 11 U.S.C. section 101 et seq., commonly known as the Bankruptcy Code, as it may be amended from time to time.

"Bankruptcy Court" has the meaning assigned to that term in the preamble to this Agreement.

"Business" has the meaning assigned to that term in the preamble to this Agreement.

"Business Day" means any day other than a Saturday, Sunday or other day on which the Bankruptcy Court is closed.

"Buyer Financing" has the meaning assigned to that term in Section 4(c).

"Closing" means the closing of the purchase and sale of the Acquired Assets pursuant to this Agreement.

"Closing Balance Sheet" has the meaning assigned to that term in Section 3(d).

"Closing Cash Payment" has the meaning assigned to that term in Section 3(b).

"Closing Date" means the time and date of the Closing determined pursuant to Section 5.

"Closing Date Statement" has the meaning assigned to that term in Section 3(d).

"Code" means the Internal Revenue Code of 1986, as amended.

"Continuing Due Diligence" has the meaning assigned to that term in this Section 1(f).

"Continuing Employees" has the meaning assigned to that term in Section 13.

"Contract" means any executory contract (as such term is used in Section 365 of the Bankruptcy Code) to which any Seller is a party (i) as of the date hereof or (ii) which is entered into by any Seller between the date hereof and the Closing Date in accordance with Section 9(d) hereof that concerns or is related to the Business, including, but not limited to, real and personal property leases, license agreements and agreements with employees, consultants or agents.

"Cure Amounts" has the meaning assigned to that term in Section 7(d).

"Current Balance Sheet" has the meaning assigned to that term in Section 7(e).

"Deposit" has the meaning assigned to that term in Section 3(a).

"DIP Lenders" means Transamerica Business Capital Corporation, f/k/a Transamerica Business Credit Corporation and the CIT Group/Business Credit, Inc.

"DIP Payment" has the meaning assigned to that term in Section 4(c).

"Disputed Items" shall have the meaning assigned to that term in Section 3(d).

"Dispute Notice" has the meaning assigned to that term in Section 3(d).

"Due Diligence Termination Date" shall mean February 18, 2002 or such later date as Buyer, upon written notice to Sellers on or before February 14, 2002, may designate (but not a date later than February 25, 2002) in order to permit Buyer to complete the due diligence contemplated by Section 12(a)(iii) (the "Continuing Due Diligence").

"Entoleter" means Entoleter, Inc., a wholly-owned subsidiary of SII.

"Environmental Laws" means Laws or Orders of any Governmental Authority relating to pollution, protection of the environment or health and safety.

"Equipment" has the meaning assigned to that term in Section 2(a)(ii).

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

"Escrow Agent" means State Street Bank and Trust Company.

"Escrow Agreement" has the meaning assigned to that term in Section 3(a).

"Estimated Net Working Capital" has the meaning assigned to that term in Section 9(b).

"Excluded Assets" has the meaning assigned to that term in Section 2(b).

"Excluded Permits" has the meaning assigned to that term in Section 2(b)(iii).

"Expense Reimbursement" has the meaning assigned to that term in Section 12(b).

"Final Working Capital Adjustment" has the meaning assigned to that term in Section 3(d)(iii).

"GAAP" means generally accepted accounting principles in the United States, consistently applied.

"Governmental Authority" means any government or any agency, bureau, commission, court, department, official, political subdivision, tribunal or other instrumentality of any government, whether federal, state or local, domestic or foreign.

"Holdback Amount" means, at any given time, \$500,000 less the aggregate dollar amount paid in respect of claims under the Post-Closing Escrow Agreement.

"Initial Deposit" has the meaning assigned to that term in Section 3(a).

"Initial Deposit Repayment" has the meaning assigned to that term in Section 3(a).

"Intellectual Property" shall mean all of the following as they exist in any jurisdictions throughout the world, in each case, to the extent owned by, licensed to, or otherwise used or held for use by Sellers:

(i) patents, patent applications, industrial rights and the inventions, designs and improvements described and claimed therein, patentable inventions, and other patent rights (including any divisionals, continuations, continuations-in-part, renewals, substitutions or reissues thereof, whether or not patents are issued on any such applications and whether or not any such applications are amended modified, withdrawn or refiled) (collectively, "Patents");

(ii) trademarks, service marks, trade dress, trade names, brand names, designs, logos or corporate names (including, in each case, the goodwill associated therewith), whether registered or unregistered, and all registrations and applications for registration thereof (collectively, "Trademarks");

(iii) copyrights, including all renewals and extensions thereof, copyright registrations and applications for registration thereof, and non-registered copyrights (collectively, "Copyrights");

(iv) trade secrets, confidential business information and other proprietary information including, without limitation, designs, research and development information, technical information, specifications, operating and maintenance manuals, methods, engineering drawings, know-how, data, mask works, discoveries, inventions, industrial designs and other proprietary rights (whether or not patentable or subject to copyright, mask work, or trade secret protection) (collectively, "Trade Secrets");

(v) all web sites and web pages and related rights and items (collectively, "Internet Assets"); and

(vi) computer software programs and software systems, including, without limitation, all databases, compilations, tool sets, compilers, higher level or "proprietary" languages, and all related material documentation and information, whether in source code, object code or human readable form (collectively "Software").

"Interim Working Capital Adjustment" has the meaning assigned to that term in Section 3(d)(i).

"Interim Working Capital Deficiency" has the meaning assigned to that term in Section 3(d)(i).

"Interim Working Capital Excess" has the meaning assigned to that term in Section 3(d)(i).

"Intertape" has the meaning assigned to that term in Section 2(b)(x).

"Inventory" has the meaning assigned to that term in Section 2(a)(iii).

"IP License(s)" shall mean all permits, licenses, sublicenses and other agreements or permissions under which any Seller is a licensee or otherwise authorized to use or practice, or under which any Seller is a licensor of, any Intellectual Property.

"Laws" means all applicable laws (including common law), statutes, rules, codes, ordinances or any requirement of any Governmental Authority.

"Letter of Intent" means the letter of intent between Buyer and Sellers dated December 31, 2001.

"Liability" has the meaning assigned to that term in Section 4(a).

"Licensed IP" means Intellectual Property that is the subject of an IP License.

"Licenses" has the meaning assigned to that term in Section 7(h)(ii).

"Liens" means any mortgage, lien, pledge, covenant restriction, security interest, claim, charge, title defect, interest and other encumbrance. Liens shall also include, in the case of the SCI Real Property, survey defects, encroachments by the SCI Real Property on real property, or interests thereon, not included in the Acquired Assets, and encroachments on SCI Real Property by buildings and improvements not included in the SCI Real Property.

"Loss" means any cost, damage, injury, expense, liability, loss, claim, deficiency or penalty of any kind or nature, including interest, penalties, and reasonable legal, accounting and other professional fees and expenses incurred in the investigation, collection, prosecution and defense of claims.

"Management Agreements" has the meaning assigned to that term in Section 9(h).

"Material Adverse Change" means events, conditions or circumstances that, individually or in the aggregate, result in or can reasonably be expected to result in, a material adverse effect on the operations, assets, or condition (financial or otherwise), of the Business, the Acquired Assets or the ability of Sellers to consummate the transactions contemplated hereby, other than as set forth on SCHEDULE 7(n) hereto.

"Material Customers" has the meaning assigned to that term in Section 7(w).

"Motion" means the "Motion of Debtors for Order Pursuant to Sections 105, 363, 365 and 1146 of the Bankruptcy Code" filed by Sellers on January 4, 2002 with the Bankruptcy Court in Sellers' chapter 11 cases, a copy of which Motion is attached to this Agreement as EXHIBIT A.

"Net Working Capital" means, at any designated time, the dollar value of Sellers' cash on hand, Inventory, Accounts Receivable, prepaid assets, refundable deposits, refundable retainers, advances to suppliers and other non-trade receivables minus the sum of (i) the amount of Assumed Obligations which would be "current liabilities" as of the



Closing, determined in accordance with GAAP applied consistently with Sellers' past practices, plus (ii) the amount of the DIP Payment.

"Net Working Capital at Closing" has the meaning assigned to that term in Section 3(d)(iii).

"Order" means any decree, injunction, judgment, order, ruling or writ of any Governmental Authority.

"Ordinary Course of Business" has the meaning assigned to that term in Section 7(g).

"Permits" means licenses, permits, franchises, approvals, authorizations, certificates of authority, and orders, or any waiver of the foregoing, issued or issuable by any Governmental Authority.

"Permitted Encumbrances" means (i) liens for current Taxes not yet due, (ii) interests of any lessors (in their capacity as such) in items constituting part of the Acquired Assets which are leased by Sellers from such lessor, (iii) assessments, rights of way and other similar non-monetary Liens, (iv) mechanics' and materialman's liens for amounts not yet due and payable, but only to the extent such liens secure Assumed Liabilities or amounts accruing after the Closing under Assigned Contracts, which do not, individually or in the aggregate, materially detract from the use or value of the Acquired Assets, and (v) the liens set forth on SCHEDULE 2(a)(i).

"Person" means any individual, corporation, partnership, limited liability company, joint venture, trust, association, unincorporated organization, other entity, or governmental body or subdivision, agency, commission or authority thereof.

"Petition" has the meaning assigned to that term in the preamble to this Agreement.

"Post-Closing Escrow Agent" means State Street Bank and Trust Company.

"Post-Closing Escrow Agreement" has the meaning assigned to that term in Section 3(b).

"Procedures Order" means an order of the Bankruptcy Court substantially in the form of the "Procedures Order" attached as an Exhibit to the Motion.

"Purchase Price" means the cash consideration paid pursuant to Section 3 plus the amount of Assumed Obligations and repayment of Sellers' debtor-in-possession financing pursuant to Section 4, subject to adjustment as provided in Section 3(d).

"Retained Liabilities" has the meaning assigned to that term in Section 4(a).

"Sale Hearing" shall mean a hearing of the Bankruptcy Court to consider the approval of this Agreement and the transactions contemplated hereby.

"Sale Order" means a final, nonappealable Order from the Bankruptcy Court, in form and substance reasonably satisfactory to Buyer, approving the sale to Buyer of the Acquired Assets contemplated hereby under Sections 363(b), 363(f) and 365 of the Bankruptcy Code free and clear of all Liens other than the Permitted Encumbrances and finding, among other things, that Buyer is a good faith purchaser entitled to the protections of Section 363(m) of the Bankruptcy Code and that the sale is covered by Section 1146(c) of the Bankruptcy Code.

"SCI" has the meaning assigned in the first paragraph hereof.

"SCI Real Property" has the meaning assigned to that term in Section 2(a)(xv).

"SCMI" has the meaning assigned in the first paragraph hereof.

"SETC" means Spinnaker Electrical Tape Company, a wholly-owned subsidiary of SII.

"SII" has the meaning assigned in the first paragraph hereof.

"Survival Termination Date" has the meaning assigned to that term in Section 14(a).

"Subsequent Deposit" has the meaning assigned to that term in Section 3(a).

"Target Net Working Capital" has the meaning assigned to that term in Section 3(d)(i).

"Taxes" means income, gross receipts, property, sales, use, license, excise, franchise, employment, social security, governmental pension or insurance, withholding or similar taxes or contributions, together with any interest, additions or penalties with respect thereto and any interest in respect of such additions or penalties.

"Termination Fee" has the meaning assigned to that term in Section 12(c).

"Transamerica Encumbrances" means the liens and encumbrances held by the DIP Lenders on any of the Acquired Assets, such liens and encumbrances to be released as of the Closing, which liens and encumbrances are listed on SCHEDULE 1(f).

## 2. PURCHASE AND SALE

(a) The Acquired Assets. Subject to the terms and conditions of this Agreement and except as provided in Section 2(b), on the Closing Date Sellers shall sell, transfer, assign and deliver to Buyer, and Buyer shall purchase and acquire from Sellers, all right, title and interest of Sellers in and to all of the assets of Sellers as of the Closing Date (other than the Excluded Assets), free and clear of Liens other than Permitted Encumbrances, including without limitation the following assets (collectively, the "Acquired Assets"):

(i) All accounts receivable, notes receivable, trade accounts, security deposits, education loans receivable and other debts due or accruing to Sellers, but excluding the items identified in Section 2(b) (collectively, the "Accounts Receivable");

(ii) All machinery, equipment, vehicles, furniture, furnishings, fixtures, operating equipment, supplies and tools, computer hardware and all parts, spares and accessories thereof and accessions thereto (collectively, the "Equipment");

(iii) All inventories of the Business, including, without limitation, raw materials, work-in-progress, finished goods, and business supplies (collectively, the "Inventory");

(iv) All cash and cash equivalents on hand and in bank accounts;

(v) All right, title and interest in and to all forms of Intellectual Property, including, without limitation, any issued patents, pending patent applications, any continuations, continuations-in-part, divisionals, reissues, reexaminations, interferences, extensions of the names, domain names, trademarks, or additions thereof, know-how, trade secrets, copyrightable works, mask works, trademarks, service marks and trade names (which for these purposes shall include "Spinnaker" or any derivation thereof, including the name "Spinnaker Electrical Tape Company," which SII shall cause SETC to transfer to Buyer);

(vi) All customer, vendor and mailing lists of Sellers, and existing telephone numbers, telecopier numbers and telex numbers used by Sellers;

(vii) All outstanding orders for the purchase of goods or services by or from Sellers;

(viii) All invoices, bills of sale and other instruments and documents evidencing Sellers' title to assets that are in the possession of Sellers;

(ix) All data processing systems, computer software, books, records, files, data bases, specifications, manuals and other papers and information of Sellers (including any and all accounting books and records, but excluding such items as are identified in clause (b)(i) below);

(x) All stationery and other imprinted material and office supplies, and packaging and shipping materials of Sellers;

(xi) All rights of Sellers under the Assigned Contracts;

(xii) To the extent their transfer is permitted by law, those Permits of Sellers listed on SCHEDULE 7(k) (except for any designated on such schedule as "Excluded Permits");

(xiii) Except for items identified in Section 2(b) below, prepaid interest and other prepaid items and deposits of any Seller as of the Closing Date, and the leasehold improvements, prepaid rent and security deposits in respect of any lease assigned to Buyer pursuant to this Agreement;

(xiv) To the extent transferable, all rights of Sellers in respect of any insurance policies (including with respect to prepaid insurance and any refund of insurance premiums paid);

(xv) All rights of recovery, rights of set-off, claims and causes of action of Sellers relating to the Business, whether known or unknown, other than those set forth in Section 2(b);

(xvi) All rights of Sellers under or pursuant to all warranties, representations and guarantees made by suppliers, manufacturers and contractors relating to the Business;

(xvii) The goodwill and other intangible assets associated with the Business; and

(xviii) To the extent not otherwise identified by items (i) - (xiv) above, real property owned by SCI (the "SCI Real Property") and described on SCHEDULE 2(a)(xviii) and other assets of Sellers described on SCHEDULE 2(a)(xviii).

(b) Excluded Assets. Notwithstanding anything to the contrary contained in this Agreement, the Acquired Assets do not include the following assets (the "Excluded Assets"):

(i) The capital stock of Sellers and the corporate seals, minute books, stock record books and other corporate records having exclusively to do with the corporate organization and capitalization of Sellers;

(ii) Contracts not constituting Assigned Contracts;

(iii) Rights under Permits designated on SCHEDULE 7(k) as "Excluded Permits";

(iv) All tax records of Sellers and all tax refunds to which any Seller is or may be entitled;

(v) To the extent not transferable, all rights of Sellers in respect of any insurance policies (including with respect to prepaid insurance and any refund of insurance premiums paid);

(vi) Any intercompany accounts receivable of Sellers from Entoleter;

(vii) The capital stock of Entoleter and all assets relating to or used by Entoleter or its business;

(viii) The capital stock of SETC and all assets of SETC (except for its trade name, which shall be an Acquired Asset);

(ix) Real property owned by SCMI;

(x) Warrants to purchase stock of Intertape Polymer Group, Inc. ("Intertape"); and

(xi) All rights relating to the claim of SII against Intertape.

(c) Assigned Contracts. At the Closing, Buyer shall acquire all right, title and interest of Sellers in and to all of the Assigned Contracts, with Cure Amounts to be allocated as provided in Section 4(b)(v).

### 3. PURCHASE PRICE AND WORKING CAPITAL ADJUSTMENT

(a) Deposit. Substantially contemporaneously with the execution of this Agreement, Buyer shall pay to the Escrow Agent, by wire transfer, the sum of \$500,000 (the "Initial Deposit") to be held in an interest-bearing escrow account subject to the terms of the Escrow Agreement substantially in the form attached hereto as EXHIBIT B, with such changes as shall be required by the Escrow Agent (the "Escrow Agreement"). On the Due Diligence Termination Date, unless Buyer has terminated this Agreement pursuant to Section 12, Buyer shall pay to the Escrow Agent, by wire transfer, the additional sum of \$1,500,000 (the "Subsequent Deposit") to also be held in said interest-bearing escrow account subject to the terms of the Escrow Agreement (together with the Initial Deposit, and the Subsequent Deposit are referred to collectively as the "Deposit"). At any time on or prior to the Due Diligence Termination Date, Buyer may, in its sole discretion, demand payment to it for any reason and at any time of the Initial Deposit. Within one (1) Business Day after such demand to the Escrow Agent, the Initial Deposit and any interest earned thereon shall be returned to the Buyer (the "Initial Deposit Repayment").

(b) Closing Payment. At the Closing, pursuant to the terms of the Escrow Agreement, in accordance with instructions of Buyer, the Escrow Agent shall pay (the "Closing Cash Payment") (i) to Sellers by wire transfer to such bank account(s) designated in writing by Sellers, an amount equal to the Deposit minus the sum of (x) the Holdback Amount and (y) the amount of the Interim Working Capital Deficiency, if any, (ii) to Buyer by wire transfer to such bank account(s) designated in writing by Buyer, (x) the amount of the Interim Working Capital Deficiency, if any, and (y) all earnings on the Deposit, and (iii) to the Post-Closing Escrow Agent in accordance with the terms of the Escrow Agreement substantially in the form attached hereto as EXHIBIT C, with such changes as shall be required by the Escrow Agent (the "Post-Closing Escrow Agreement"), the Holdback Amount. In addition, in the event that there is an Interim Working Capital Excess, Buyer shall pay to Sellers at the Closing by wire transfer to such bank accounts designated by Sellers an amount equal to the Interim Working Capital Excess. If this Agreement is terminated after payment of the Deposit for any reason whatsoever, the Deposit and any interest earned thereon (minus \$500,000 in the event that Sellers are entitled

to liquidated damages as described in Section 3(e)) shall be returned to Buyer within one (1) Business Day of demand by Buyer to the Escrow Agent.

(c) Allocation of Purchase Price. Sellers and Buyer shall allocate the aggregate purchase price to be paid for the Acquired Assets in accordance with Section 1060 of the Code. Sellers and Buyer shall use reasonable best efforts to agree upon such allocation and reduce it to writing as soon as practicable following the execution of this Agreement, and in any event at least 7 days before the Auction Date; such allocation shall be attached to this Agreement as SCHEDULE 3(c). In addition, Sellers and Buyer hereby undertake and agree to file timely any information that may be required to be filed pursuant to Treasury Regulations promulgated under Section 1060(b) of the Code. Neither Sellers nor Buyer shall file any tax return or other document or otherwise take any position which is inconsistent with any allocation agreed upon by them.

(d) Working Capital Adjustments.

(i) Attached hereto as SCHEDULE 3(d)(i) is Sellers' projected statement of Net Working Capital as of February 28, 2002 (the "Target Net Working Capital"). Within five Business Days before the Closing Date, Sellers shall deliver to Buyer a written estimate of the Net Working Capital as of the Closing Date, which such estimate shall be calculated in good faith by Sellers and which shall be accompanied by a reasonably detailed schedule showing the calculation thereof (the "Estimated Net Working Capital"). If the Estimated Net Working Capital exceeds the Target Net Working Capital by an amount greater than \$350,000 and Buyer does not elect to terminate this Agreement pursuant to Section 12(a)(vi) hereof, then the Purchase Price shall be increased by an amount equal to (x) the amount by which the Estimated Net Working Capital exceeds the Target Net Working Capital minus (y) \$350,000 (the "Interim Working Capital Excess"). If the Target Net Working Capital exceeds the Estimated Net Working Capital by an amount greater than \$350,000 and Sellers do not elect to terminate this Agreement pursuant to Section 12(a)(vii) hereof, then the Purchase Price shall be decreased by an amount equal to (x) the amount by which the Target Net Working Capital exceeds the Estimated Net Working Capital minus (y) \$350,000 (the "Interim Working Capital Deficiency"). In the event of any Interim Working Capital Excess or Interim Working Capital Deficiency, the Closing Payment shall be adjusted as provided in Section 3(b) (such adjustments to the Closing Payment and the Purchase Price, the "Interim Working Capital Adjustment").

(ii) Within 60 days following the Closing Date, Buyer will prepare and deliver to Sellers a statement (the "Closing Date Statement"), certified in writing by Ernst & Young, containing Buyer's calculation of Sellers' Net Working Capital at Closing. Unless Buyer shall have received a written notice from Sellers (the "Dispute Notice") prior to the close of business on the tenth Business Day following Sellers' receipt of the Closing Date Statement which disputes Buyer's calculation of Sellers' Net Working Capital at Closing set forth therein and which sets forth in reasonable detail the items of dispute (the "Disputed Items"), Buyer's calculation of Sellers' Net Working Capital at Closing set forth on the Closing Date Statement shall be binding for all purposes of this Agreement. In the event that Sellers have delivered a

Dispute Notice to Buyer in accordance with this Section 3(d), Buyer and Sellers shall negotiate in good faith to resolve the Disputed Items and agree upon the amount of Sellers' Net Working Capital at Closing and any items not identified in Sellers' Dispute Notice and that are not affected by the determination of any Disputed Items shall be final and binding and shall not be subject to further negotiation between the parties. In the event that Buyer and Sellers fail to agree on the Disputed Items and the amount of Sellers' Net Working Capital at Closing within 14 Business Days following the date of the Dispute Notice, Buyer and Sellers hereby agree that the final determination of the amount of Sellers' Net Working Capital at Closing shall be made by Deloitte Touche (the "Accountant"). The Accountant shall resolve the Disputed Items and determine Sellers' Net Working Capital at Closing based solely on the written submissions and presentations by Sellers and Buyer, and not by independent review. Buyer and Sellers shall instruct the Accountant to make a determination with respect to the Disputed Items and report such determination to the parties within 15 Business Days after the date of their submission. The Accountant's resolution of the Disputed Items and determination of Sellers' Net Working Capital at Closing shall be final and binding on the parties, and a judgment may be entered thereon in any court of competent jurisdiction. Each party shall be responsible for the fees and disbursements of the Accountant in the same proportion that (x) the aggregate amount of the Disputed Items with respect to which such party was the non-prevailing party (as finally determined by the Accountant) bears to (y) the aggregate amount of all Disputed Items. Buyer and Sellers agree to execute, if requested by the Accountant, an engagement letter upon terms and conditions that are reasonable and otherwise customary for transactions similar in nature.

(iii) If the Net Working Capital at Closing as finally determined pursuant to the previous paragraph (the "Net Working Capital at Closing") exceeds the Target Net Working Capital and the amount of such excess is greater than \$350,000, then the Purchase Price, as may have been adjusted at Closing pursuant to the Interim Working Capital Adjustment, shall be finally increased (or decreased as the case may be) by an amount equal to (x) the amount by which the Net Working Capital at Closing exceeds the Target Net Working Capital minus (y) \$350,000, all as adjusted upward or downward to give effect to the Interim Working Capital Adjustment. If the Net Working Capital at Closing is less than the Target Net Working Capital and the amount of such deficiency is greater than \$350,000, then the Purchase Price, as may have been adjusted at Closing pursuant to the Interim Working Capital Adjustment, shall be finally decreased (or increased as the case may be) by an amount equal to (x) the amount by which the Net Working Capital at Closing is less than the Target Net Working Capital minus (y) \$350,000, all as adjusted upward or downward to give effect to the Interim Working Capital Adjustment. Either final adjustment referred to in this Section 3(d)(iii) is referred to as the "Final Working Capital Adjustment." Any amount to which Sellers are entitled pursuant to the Final Working Capital Adjustment shall be paid no later than five (5) Business Days after the determination of the Final Working Capital Adjustment by wire transfer of immediately available funds to an account or accounts designated in writing by Sellers. Any amount to which Buyer is entitled pursuant to the Final Working Capital Adjustment shall be paid from the Holdback Amount pursuant to the terms of the Post-Closing Escrow Agreement.

(iv) In the event that a Final Working Capital Adjustment is not required under Section 3(d)(iii) but there was an Interim Working Capital Excess or Interim Working Capital Deficiency, then the adjustments made to the Purchase Price due to the Interim Working Capital Excess or Interim Working Capital Deficiency, as the case may be, shall be reversed in whole or in part and the Purchase Price shall be appropriately adjusted.

(e) Liquidated Damages. The parties hereby agree that it is impossible to determine accurately the amount of damages that Sellers would suffer if the transactions contemplated herein were not consummated as a result of a material breach of this Agreement by Buyer. As a result, notwithstanding anything in this Agreement to the contrary, the parties hereby agree that (i) in the event of a failure by Buyer to consummate the transactions contemplated herein as a result of a breach of its obligations under this Agreement and termination of this Agreement by Sellers in accordance with Section 12 hereof, Buyer shall be obligated to pay liquidated damages in the amount of \$500,000 and (ii) such liquidated damages shall be the sole and exclusive remedy of Sellers against Buyer by reason of such breach and such termination. Accordingly, if liquidated damages are payable hereunder, the Escrow Agent shall deliver \$500,000 of the Deposit to the Sellers, and shall deliver the balance of the Deposit and any earnings thereon to the Buyer, provided, that nothing herein shall limit the right of Buyer, at any time on or prior to the Due Diligence Termination Date, to the return, at its request, of the Initial Deposit and any interest earned thereon pursuant to Section 3(a).

#### 4. LIABILITIES AND OBLIGATIONS

(a) Non-Assumption of Liabilities. Notwithstanding anything to the contrary contained herein and except as expressly set forth in Section 4(b), Buyer does not assume and shall have no responsibility or obligation whatsoever for any liabilities, commitments or obligations of Sellers of any kind or nature whatsoever, known or unknown, accrued, fixed, contingent or otherwise, liquidated or unliquidated, choate or inchoate, due or to become due ("Liabilities") including, without limitation, any liabilities or obligations in respect of any intercompany accounts payable of Sellers to Entoleter or liabilities associated with any Excluded Assets (collectively, the "Retained Obligations").

(b) Assumed Obligations. At the Closing, subject to the limitation set forth in Section 4(c), Buyer shall assume the following liabilities and obligations (the "Assumed Obligations") of Sellers:

(i) post-Petition trade payables and liabilities incurred in the Ordinary Course of Business consistent with present practice in Sellers' chapter 11 cases (including an aggregate of up to \$1,250,000 for court-retained professionals' fees and reimbursement of Sellers for court-approved amounts already paid, but excluding (x) any such professionals' fees in excess of such amount and (y) any amounts payable to Deloitte Touche under Section 3 of this Agreement);

(ii) Sellers' accrued pre-Petition liabilities for vacation, payroll, payroll Taxes, real estate and personal property Taxes, customer claims and rebates as set



forth on SCHEDULE 4(b)(ii) in an amount not to exceed \$2,593,000, to the extent approved by the Bankruptcy Court and not satisfied before Closing;

(iii) key employee retention bonuses approved by the Bankruptcy Court in an amount not to exceed \$750,000, and obligations under employee Contracts set forth on SCHEDULE 7(d);

(iv) certain other pre-Petition liabilities set forth on SCHEDULE 4(b)(iv) in an amount not to exceed \$2,475,000, to the extent approved by the Bankruptcy Court and not satisfied before Closing;

(v) the liabilities and obligations of Sellers under the Assigned Contracts that have accrued as of the Closing Date, including all Cure Amounts with respect thereto (except for Cure Amounts the payment of which would cause the Assumed Liabilities and DIP Payments to exceed \$23,763,000, in which case Sellers shall make payments to the extent necessary to prevent such excess) and liabilities and obligations of Sellers under purchase orders and supply contracts; and

(vi) other post-Petition liabilities and obligations that have accrued as of the Closing Date in the Ordinary Course of Business, including but not limited to employee-related obligations such as 401(k), pension, health insurance, etc. (but not with respect to employees of SCMI).

(c) Proceeds of Buyer Financing. The parties hereto acknowledge that Buyer contemplates arranging for the DIP Lenders to provide revolving and term credit facilities on terms and conditions equivalent to Sellers' existing financing or with modifications thereto acceptable to Buyer in its sole discretion (the "Buyer Financing"). Buyer shall use all or a portion of the proceeds of the Buyer Financing (and any other funds required) to repay the total amount of principal, accrued interest and other charges on Sellers' debtor in possession financing with the DIP Lenders at Closing (the "DIP Payment").

(d) Limitation on Assumed Obligations. Notwithstanding the above, in no event shall the aggregate amount of the Assumed Obligations as of the Closing Date (excluding (i) obligations under the employee Contracts set forth on Schedule 7(d) that will not be due and payable as of the Closing and that relate to the period subsequent to the Closing and (ii) liabilities under Assigned Contracts and other post-Petition obligations assumed by Buyer that, in each case, relate to the period subsequent to the Closing which would not be "current liabilities" as of the Closing under GAAP applied consistently with past practices) and the DIP Payment exceed \$23,763,000. In the event that the aggregate amount of the Assumed Obligations (other than those excluded in the parenthetical of the first sentence of this paragraph) as of the Closing Date and the DIP Payment would otherwise exceed \$23,763,000 (after giving effect to payment of any Cure Amounts by Sellers pursuant to Section 4(b)(v)), a portion of the Assumed Obligations (other than those excluded in the parenthetical of the first sentence of this paragraph) shall be redesignated as Retained Obligations such that the aggregate amount of Assumed Obligations (other than those excluded in the parenthetical of the first sentence of this paragraph) as of the Closing Date and the DIP Payment equals \$23,763,000. Buyer shall have the right, in its sole discretion, to determine which Assumed Obligations (other than those

excluded in the parenthetical of the first sentence of this paragraph) shall be redesignated as Retained Obligations pursuant to the preceding sentence.

(e) Rejection of Contracts. Sellers shall timely reject any Contracts identified on SCHEDULE 7(d) for rejection (or which are otherwise determined not to be Assigned Contracts pursuant to the definition thereof). Notwithstanding the above, Sellers shall not be required to reject SCMI's lease with Sappi Fine Paper North listed on SCHEDULE 7(d). Buyer shall not be liable for any claims arising from the rejection or retention of such Contracts.

5. OBTAINING OF PROCEDURES AND SALE ORDER; CLOSING

(a) Obtaining Order. Sellers shall use their reasonable best efforts to obtain entry of the Procedures Order and the Sale Order, subject to its obligations under the Bankruptcy Code.

(b) Closing. If the Sale Order is entered, then, subject to the satisfaction or waiver by the parties of the conditions to their respective obligations to effect the Closing set forth in Sections 10 and 11, the Closing shall take place at the offices of Paul, Weiss, Rifkind, Wharton & Garrison at 10:00 a.m. (New York time) within two Business Days following the date that the Sale Order has become final.

6. DELIVERIES AT CLOSING

(a) Deliveries by Seller. At the Closing, Sellers shall deliver, or cause to be delivered (in addition to any other instruments required by Section 10 or otherwise by this Agreement to be delivered by Sellers at the Closing), to Buyer the following (in form and substance reasonably satisfactory to Buyer):

(i) limited warranty deeds transferring title to and interest in the SCI Real Property to Buyer;

(ii) a duly executed bill or bills of sale and assignment or other appropriate instruments transferring title to and interest in all of the Acquired Assets to Buyer;

(iii) appropriate (in both number and form) executed originals of amendments to the certificates of incorporation of SII, SCI, SCMI and SETC changing their names to names not using the name "Spinnaker" or any name that is similar thereto, together with checks from Sellers in appropriate amounts necessary for the filing and recording thereof in the appropriate state governmental office;

(iv) a certified copy of the Sale Order;

(v) possession of all of the Acquired Assets;

(vi) evidence reasonably satisfactory to Buyer of compliance with the notice provisions set forth in the Procedures Order and in the Sale Order;

(vii) evidence reasonably satisfactory to Buyer of the transfer or reissuance to Buyer of the Permits listed on SCHEDULE 7(k) (other than Excluded Permits);

(viii) copies of the resolutions of the Board of Directors of each of the Sellers authorizing the execution and performance by such Seller of this Agreement and authorizing the officers of such Seller to carry out and perform the terms and provisions hereof, certified by an appropriate officer of such Seller; and

(ix) such other instruments or documents as Buyer may reasonably request to fully effect the transfer of the Acquired Assets and to confer upon Buyer the benefits contemplated by this Agreement.

(b) Deliveries by Buyer. At the Closing, Buyer shall deliver, or cause to be delivered (in addition to any other instruments required by Section 11 or otherwise by this Agreement to be delivered by Buyer at the Closing), to Sellers, the following:

(i) the Purchase Price payable in the manner described in Section 3; and

(ii) a duly executed Assignment and Assumption Agreement in form and substance reasonably satisfactory to Sellers, whereby Buyer will assume and agree to pay, perform and discharge the Assumed Obligations.

#### 7. REPRESENTATIONS AND WARRANTIES OF SELLERS

Sellers hereby jointly and severally represent and warrant to Buyer as follows:

(a) Organization; Authorization. Each Seller is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and, subject to entry of the Sale Order, has the requisite corporate power and authority to execute and deliver this Agreement and to perform its obligations hereunder. Subject to entry of the Sale Order, the execution, delivery and performance of this Agreement have been duly authorized by all necessary corporate action of Sellers. This Agreement has been duly and validly executed by each Seller and, subject to the entry of the Sale Order, constitutes a legal, valid and binding obligation of each Seller, enforceable against it in accordance with its terms.

(b) No Conflict; Consents. Subject to the entry of the Sale Order and except as otherwise set forth on SCHEDULE 7(b), neither the execution and delivery of this Agreement nor the consummation of any or all of the transactions contemplated hereby will (i) violate the certificate of incorporation or by-laws (or other governing instrument) of any Seller; (ii) violate, be in conflict with or constitute a default under, or require the consent of any third party to, any Assigned Contract; or (iii) violate any Laws or Orders applicable to the Business.

(c) Consents and Approvals of Governmental Authorities. Other than the entry of the Sale Order by the Bankruptcy Court, no consent, approval or authorization of, or declaration, filing or registration with, any Governmental Authority is required in connection

with the execution, delivery and performance of this Agreement or the consummation of the transactions contemplated hereby.

(d) Contracts. SCHEDULE 7(d) sets forth a list of all Contracts. In the event Buyer identifies any Contracts not listed on SCHEDULE 7(d) as executory contracts (as such term is used in Section 365 of the Bankruptcy Code), then Sellers shall amend SCHEDULE 7(d) to include such Contracts. Upon the written request of Buyer, Sellers shall, at least 7 days prior to the Due Diligence Termination Date, provide Buyer with a list of all amounts required, to the best knowledge of Sellers, to cure all defaults under each of the Contracts designated by Buyer in such request, so as to permit the assumption and assignment of each such Contract pursuant to Section 365 of the Bankruptcy Code (the "Cure Amounts"). Copies of all written Contracts have been made available to Buyer. Except as otherwise set forth on SCHEDULE 7(d), all of the Contracts are valid, binding and enforceable in accordance with their terms, and are in full force and effect. Except as set forth on SCHEDULE 7(d) and in the case of Seller, except for defaults of the type referred to in Section 365(b)(2) of the Bankruptcy Code, there are no material defaults (or events that, with notice or lapse of time or both, would constitute a material default) by any Seller, or to the knowledge of Sellers, any other party under any of the Contracts.

(e) Financial Statements. Sellers have delivered to Buyer the audited consolidated balance sheet and income statement of SII for the fiscal year ended December 31, 2000 (the "Audited Financials") attached as SCHEDULE 7(e)(i) hereto and the interim unaudited balance sheet of SCI and SCMI for the fiscal period ended September 30, 2001 attached as SCHEDULE 7(e)(ii) hereto (the "Current Balance Sheet"). The Audited Financials fairly and accurately reflect the financial position of Sellers on a consolidated basis (including Entoleter) as of the dates thereof, and have been prepared in accordance with GAAP consistently applied during the periods involved, except as indicated in the notes thereto. The Current Balance Sheet fairly and accurately reflects the financial position of SCI and SCMI as of the date thereof, and have been prepared in accordance with GAAP consistently applied during the periods involved, subject to the absence of footnotes and year-end adjustments (including adjustments resulting from Sellers' chapter 11 cases).

(f) Equipment. Set forth on SCHEDULE 7(f) is a complete and correct list of all Equipment as of October 31, 2001. Such Equipment is sufficient to operate the Business as operated prior to November 13, 2001. The Equipment which is necessary to operate the Business as operated prior to the November 13, 2001 is in good operating condition and repair, subject to normal wear and tear.

(g) Inventory. With respect to the Business, the amount of Inventory on hand (i) has been manufactured and/or purchased in the ordinary course of business, consistent with past custom and practice (the "Ordinary Course of Business"); and (ii) is not obsolete and is of a quality usable and saleable in the Ordinary Course of Business, other than with respect to reserves maintained by Sellers for obsolete or "slow moving" inventory.

(h) Intellectual Property.

(i) SCHEDULE 7(h) sets forth the following items owned or licensed by Sellers or otherwise used or held for use by Sellers: (i) all U.S. and foreign

issued patents and utility patents, and all pending patent applications relating to any inventions, and all reissues, divisions, continuations, continuations-in-part, extensions, reexaminations or interferences of them; (ii) all U.S. and foreign registered trademarks, registered service marks, trademark and service mark applications, unregistered trademarks and service marks, trade names and logos; (iii) all U.S. and foreign registered copyrights and copyright applications and all renewals and extensions; and (iv) a general identification of all logos and domain name addresses.

(ii) SCHEDULE 7(h) sets forth all material IP Licenses granted by or to any Seller and all other material agreements to which any Seller is a party, which create rights in such Seller or in any third party regarding any Intellectual Property specifically or other intellectual property generally. The IP Licenses are binding against the Seller and in full force and effect. The continued use by Buyer of any IP License or Licensed IP is not restricted by any IP License.

(iii) Except as set forth on SCHEDULE 7(h), Sellers are the owners, free and clear of all liens, claims and encumbrances (except Permitted Encumbrances and Transamerica Encumbrances), of all right, title and interest in the Intellectual Property (except for Licensed IP) and Sellers have the absolute right to use and assign those rights without seeking the approval or consent of any third party and without payments to any third party. The Intellectual Property constitutes all of the intellectual property necessary to conduct the Business as it is presently conducted or anticipated to be conducted. All registrations and applications for the Intellectual Property are in full force and effect. There are no existing or, to the knowledge of Sellers, threatened claims or proceedings by any Person and there is no basis for any claim or proceeding relating to the use by Sellers of the Intellectual Property or challenging its ownership of the same. Except as set forth on SCHEDULE 7(h), to the knowledge of Sellers, there are no infringing or diluting uses of the Intellectual Property, and no investigations are pending concerning the possibility of such infringing or diluting use.

(iv) To the knowledge of Sellers, no Seller has interfered with, infringed upon, misappropriated, or otherwise come into conflict with any intellectual property rights of third parties, and, except as set forth on SCHEDULE 7(h), no Seller has received any charge, complaint, claim, or notice alleging any such interference, infringement, misappropriation or violation and there is no basis for any such claim.

(v) Sellers have taken commercially reasonable steps to maintain the confidentiality of their Trade Secrets.

(vi) Each present or past employee, officer, consultant or any other person who developed any part of any material Intellectual Property has vested in a Seller any and all right, title and interest in and to all such Intellectual Property.

(vii) All material Software owned or licensed by Sellers for use in the Business or necessary for the conduct of the Business as currently conducted or anticipated to be conducted is set forth in SCHEDULE 7(h).

(viii) The execution of this Agreement will not result in the loss or impairment of the rights of Buyer to own or use any of the Intellectual Property.

(ix) Sellers products relating to the Business have been marked as required by the applicable Patent statute and Sellers have given the public notice of its Copyrights and notice of its Trademarks as required by the applicable Trademark and Copyright statutes.

(i) Compliance with Law. Except as set forth on SCHEDULE 7(i), (i) the operations of the Business have been conducted and are in all material respects in accordance with all applicable Laws (including all Environmental Laws) of all Governmental Authorities having jurisdiction over Sellers and applicable to the Acquired Assets and (ii) no Seller has received any notification of any asserted present or past failure by any Seller to comply with any such Laws during the past three (3) years which apply to the operation of the Business.

(j) Books and Records. All of the books of account and other records of Sellers relating to the Acquired Assets and the Business have been made available to Buyer. To the best knowledge of Sellers, such books and records are complete and correct in all material respects.

(k) Permits. Set forth on SCHEDULE 7(k) is a complete list of all of Sellers' material Permits relating to the Acquired Assets and the Business. Except as set forth on SCHEDULE 7(k), such Permits (i) are valid and effective, (ii) represent all material Permits required by any Governmental Authority with jurisdiction over the Acquired Assets to own and operate the Acquired Assets in connection with the Business in the same manner as operated prior to the date hereof and (iii) may be transferred or reissued to Buyer without the approval of any third party.

(l) Environmental Matters. Except as set forth on SCHEDULE 7(l), there are no events, conditions or circumstances which have resulted or are reasonably likely to result in liability pursuant to Environmental Laws or principles of common law relating to pollution, protection of the environment or health and safety.

(m) Employees. Set forth on SCHEDULE 7(m) is the following: (i) a listing of the names, titles and dates of hire of all of the employees of Sellers who are not governed by any collective bargaining agreement, (ii) a list of collective bargaining agreements entered into by Sellers and (iii) a list of all "employee benefit plans" (within the meaning of Section 3(3) of ERISA), whether or not subject to ERISA, in which current or former employees of the Business participate. The annual salaries and bonuses of such employees of Sellers and a copy of such collective bargaining arrangements and employee benefit plans have been made available to Buyer on or prior to the date hereof.

(n) Absence of Certain Changes. Except as set forth in SCHEDULE 7(n), since September 30, 2001: (i) there has been no Material Adverse Change; (ii) there has been no damage, destruction or loss to any material asset or property, tangible or intangible, of Sellers, ordinary wear and tear excepted; (iii) other than in connection with the proposed sale of the Acquired Assets and the Business, the Business has been conducted only in the Ordinary Course

of Business; (iv) no Seller has increased the compensation of any officer or granted any general salary or benefits increase to their employees other than in the Ordinary Course of Business; (v) the post-Petition liabilities have been paid in the Ordinary Course of Business; and (vi) there has been no change by Sellers, in relation to the Business or in accounting principles, practices or methods.

(o) Liabilities. Sellers do not have any Liabilities other than (i) Liabilities as set forth in the Current Balance Sheet or referred to in the footnotes to the Audited Financials, (ii) Liabilities set forth in SCHEDULE 7(o) and (iii) Liabilities incurred after September 30, 2001 in the Ordinary Course of Business.

(p) Insurance. SCHEDULE 7(p) contains an accurate summary description of all policies of property, fire and casualty, product liability, workers compensation and other forms of insurance owned by or held by any Seller in connection with the Business, together with a list of all material outstanding claims against any insurer relating to the Business. Except as set forth on SCHEDULE 7(p), no Seller has received (a) any notice of cancellation or non-renewal of any policy described in such SCHEDULE 7(p) or refusal of coverage thereunder, (b) any notice that any issuer of such policy has filed for protection under applicable insolvency laws or is otherwise in the process of liquidating or has been liquidated, or (c) any other indication that such policies are no longer in full force or effect or that the issuer of any such policy is no longer willing or able to perform its obligations thereunder.

(q) Taxes. All Tax returns, reports and forms of Sellers due prior to the date hereof with respect to the Business have been timely filed and properly reflect the tax liability of Sellers with respect to the applicable periods, and no extension of time with respect to any date on which any Tax return, report or form was or is to be filed with respect to Sellers is in force. All Taxes and withholding amounts due and payable (or required to be withheld) prior to the date hereof have been paid (or withheld). Except as set forth on SCHEDULE 7(q), no claim for any Taxes has been proposed, threatened in writing or assessed against any Seller and, to Sellers' knowledge, no facts exists that make such a claim likely. Except as set forth on SCHEDULE 7(q), no ongoing audit, litigation or similar proceeding concerning any Tax returns of any Seller with respect to the Business or the Acquired Assets has been proposed, threatened, or is in progress nor does there exist any waiver or agreement for the extension of time for the assessment of any Taxes against any Seller with respect to the Business or the Acquired Assets. Except as set forth on SCHEDULE 7(q), there are no Liens on any of the Acquired Assets that arose in connection with any failure (or alleged failure) to pay any Tax and there are no claims for Taxes, and no basis for which any such claims might be made, that might result in any such Liens. No claim has ever been made by a taxing authority in a jurisdiction where Sellers do not currently file Tax returns that any Seller is or may be subject to taxation by such jurisdiction. None of the Acquired Assets is a "tax exempt use property" within the meaning of Section 168(h) of the Code. None of the Acquired Assets is subject to a lease made pursuant to Section 168(f)(8) of the Internal Revenue Code of 1954.

(r) Accounts Receivable. The Accounts Receivable constitute bona fide, valid and collectible claims arising in the Ordinary Course of Business in a manner consistent with Sellers' normal credit practices and are subject to no set-offs or counterclaims (other than

returns in the Ordinary Course of Business), subject only to reasonable reserves for bad debts calculated in a manner consistent with Sellers' past practice.

(s) Brokers; Agents. Except with respect to FTI Policano & Manzo, Sellers have not dealt with any agent, finder, broker or other representative in any manner which could result in Buyer being liable for any fee or commission in the nature of a finder's fee or originator's fee in connection with the subject matter of this Agreement.

(t) Warranty Obligations. SCHEDULE 7(t) contains a true and complete description of Sellers' experience over the past three years with respect to product warranty obligations, pricing and other accommodations. To the best of Sellers' knowledge, as of September 30, 2001, sufficient reserves were maintained on the books of Sellers to cover Sellers' product warranty obligations. Over the past three years, Sellers have had no product recall obligations.

(u) Real Property. SCI owns good and marketable fee title to the SCI Real Property. At the Closing Date, such title shall be free and clear of all Liens other than Permitted Encumbrances. Except as set forth in SCHEDULE 7(u), the SCI Real Property constitutes all of the real property used by any of Sellers in the conduct of the Business. Each parcel included in the SCI Real Property constitutes a separate tax lot. There is no pending or, to Sellers' knowledge, threatened condemnation (or any sale in lieu thereof) affecting the SCI Real Property.

(v) Litigation. Except as set forth on SCHEDULE 7(v) or claims made in connection with Sellers' chapter 11 cases, there are no material actions, claims, causes of action, proceedings, suits or investigations pending or, to the knowledge of Sellers, threatened, against Sellers or any of their respective assets, properties or rights, before any Governmental Authority. None of the Sellers is subject to any Order entered in any lawsuit or proceeding.

(w) Trade Relations. On or prior to the date hereof, Sellers have delivered to Buyer a list of SCI's ten largest customers (as determined by the dollar amount of sales to such customers for the year ending December 31, 2001) (the "Material Customers"). There exists no actual or, to the knowledge of Sellers, threatened, cancellation of, or (except for the tightening of credit terms as a result of Sellers' chapter 11 cases) any material adverse modification to or change in, the business relationship of Sellers with any Material Customer or material supplier.

(x) Accuracy of Representations. The representations and warranties made by Sellers herein and the other information contained in the schedules attached hereto contain no untrue statement of a material fact or omit to state a material fact necessary in order to make the statements contained herein and therein not misleading. Sellers are not aware of any fact, event, circumstance or condition that could reasonably be expected to result in a Material Adverse Change that has not been disclosed in writing to Buyer.

(y) TERMS OF SALE. EXCEPT AS OTHERWISE SPECIFICALLY SET FORTH IN THIS AGREEMENT, THE ACQUIRED ASSETS ARE BEING SOLD TO BUYER ON AN "AS-IS, WHERE IS" BASIS, WITHOUT WARRANTY. SELLERS HEREBY DISCLAIM ALL OTHER WARRANTIES, EXPRESS OR IMPLIED, INCLUDING THE IMPLIED WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR



PURPOSE. BUYER HEREBY ACKNOWLEDGES AND AGREES THAT BUYER, AND ITS SUCCESSORS AND ASSIGNS, SHALL BEAR ALL RISKS OF INJURY OR DAMAGE TO PERSONS OR PROPERTY TO THE EXTENT RELATING TO THE OPERATION OF THE ACQUIRED ASSETS ON AND AFTER THE CLOSING DATE.

8. REPRESENTATIONS AND WARRANTIES OF BUYER

Buyer represents and warrants to Sellers as follows:

(a) Organization of Buyer; Authorization. Buyer is a limited liability company or other entity duly organized, validly existing and in good standing under the laws of the State of Delaware and, has the requisite organizational power and authority to execute and deliver this Agreement and to perform its obligations hereunder. The execution, delivery and performance of this Agreement have been duly authorized by all necessary organizational action of Buyer. This Agreement has been duly and validly executed by Buyer and, subject to the entering of the Sale Order by the Bankruptcy Court, constitutes a legal, valid and binding obligation of Buyer, enforceable against it in accordance with its terms.

(b) No Conflict as to Buyer. Except as otherwise set forth on SCHEDULE 8(b), neither the execution and delivery of this Agreement nor the consummation of any or all of the transactions contemplated hereby will (i) violate the articles of organization or operating agreement (or other governing instrument) of Buyer; (ii) violate, be in conflict with, or constitute a default under, or require the consent of any third party to, any material contract or other agreement to which Buyer is a party; or (iii) to the knowledge of Buyer, violate any statute, law or regulation of any Governmental Authority applicable to Buyer.

(c) Brokers; Agents. Buyer has not dealt with any agent, finder, broker or other representative in any manner which could, solely as a result of action by Buyer, result in Sellers being liable for any fee or commission in the nature of a finder's fee or originator's fee in connection with the subject matter of this Agreement.

9. ADDITIONAL AGREEMENT OF THE PARTIES

(a) Physical Inventory. Sellers shall continue their practice of periodic cycle counts of the Inventory through the Closing Date. If such cycle counts result in either increases or decreases to Inventory balances, such adjustments shall be reflected in the calculation of the Estimated Net Working Capital (as defined below) and the Closing Date Statement.

(b) Reasonable Best Efforts.

(i) Upon the terms and subject to the conditions of this Agreement, Buyer and Sellers will use their reasonable best efforts to take, or cause to be taken, all action, and to do, or cause to be done, all things necessary, proper or advisable consistent with applicable law to cause the conditions precedent to Closing to be satisfied and to cause to the Closing to occur on or prior to the date set forth in Section 12(a)(i), including, without limitation, to obtain the consent or approval of any third party or Governmental Authority necessary to consummate the transactions contemplated hereby

in accordance with the terms hereof and, in the case of Buyer, to timely obtain the Buyer Financing; provided, that (i) nothing herein shall obligate Buyer to accept financing under terms and conditions more onerous than those currently provided by the DIP Lenders to Sellers and (ii) Buyer may, in its sole discretion, seek financing from parties other than the DIP Lenders, but shall not be obligated to seek such financing in order to comply with this Section 9(b)(i).

(ii) Each Seller agrees that it will promptly take such actions as are reasonably intended to obtain the Bankruptcy Court's approval of the Sale Order, including, without limitation, demonstrating that (x) Buyer is a "good faith" purchaser under Section 363(m) of the Bankruptcy Code, (y) Buyer has provided adequate assurance of future performance as assignee of the Assigned Contracts and (z) Section 363(f) of Bankruptcy Code shall apply to the sale of the Acquired Assets. In the event that stay of the Sale Order is sought or any of such Orders are appealed, Sellers shall use their reasonable best efforts to oppose such request for a stay or defend any such appeal, as applicable. Buyer shall provide Sellers with all information reasonably requested by Sellers in connection with such actions.

(iii) Sellers will provide Buyer with copies of all motions, applications and supporting papers prepared by Sellers (including forms of the Sale Order and other orders and notices to interested parties) relating to Buyer, this Agreement or the Acquired Assets prior to the filing thereof in the Bankruptcy Court, shall consult with Buyer and its counsel with respect thereto, and shall incorporate therein such changes or additions as Buyer may reasonably request. In connection with the Sale Order, Seller shall seek and obtain Buyer's approval of such order (such approval not to be unreasonably withheld).

(iv) Sellers shall give appropriate notice, and provide appropriate opportunity for hearing, to all parties entitled thereto, of all motions, orders, hearings or other proceedings relating to this Agreement.

(v) Sellers shall give prompt notice to Buyer, and Buyer shall give prompt notice to Sellers, of (x) the occurrence, or failure to occur, of any event that would be likely to cause any representation or warranty contained in this Agreement to be untrue or inaccurate in any material respect at any time from the date of this Agreement to the Closing Date, and (y) any failure of Buyer or any Seller, as the case may be, to comply with or satisfy, in any material respect, any covenant, condition or agreement to be complied with or satisfied by it under this Agreement.

(c) Access; Records; Bankruptcy Papers. From and after the date hereof, authorized representatives of Buyer (including its accountants, advisors, potential financing sources, consultants and legal counsel) shall have the right, upon reasonable notice and at reasonable times, to inspect the Acquired Assets and their condition and shall be provided reasonable access to Sellers' officers, advisors, counsel, trade vendors, customers, properties, and facilities, including for the purpose of environmental sampling, and, provided, that Buyer shall not take any action which unreasonably interferes with Sellers' operation of the Business prior to the Closing Date in any material respect. From and after the date hereof, Sellers shall

give Buyer and its authorized representatives, full access to their books and records relating to the Business, as Buyer may reasonably request, permit Buyer to make inspections thereof, and cause Sellers' officers and advisors to furnish Buyer with such financial, tax and other operating data and other information as Buyer may reasonably request (subject to Buyer's execution of customary confidentiality and similar agreements). Sellers hereby agree that they will retain, until all appropriate statutes of limitations (including any extensions) expire, copies of all tax returns and supporting work schedules and other records or information which may be relevant to such tax returns, except for such tax returns, supporting work schedules and other records which Buyer shall acquire as a consequence of this Agreement (provided, that Sellers may elect not to retain any such copies if they give such copies or make such copies available to Buyer), and that they will not destroy or otherwise dispose of such materials without first providing Buyer with a reasonable opportunity to review and copy such materials. Buyer hereby agrees that it will retain, until all appropriate statutes of limitations (including any extensions) expire, copies of all tax returns and supporting work schedules received from any Sellers pursuant to this Agreement and other records or information which may be relevant to such tax returns (provided, that Buyer may elect not to retain any such copies if Buyer gives such copies or makes such copies available to Sellers), and that it will not destroy or otherwise dispose of such materials without first providing Sellers with a reasonable opportunity to review and copy such materials. After the Closing Date, Buyer shall give Sellers and their authorized representatives full access to the books and records acquired as a consequence of this Agreement for purposes of and relating to the prosecution of any claims of Sellers or which may otherwise be needed to enforce their remaining rights and defend their remaining obligations relating to the Acquired Assets and the Business or in connection with Sellers' chapter 11 cases. Sellers will promptly deliver to Buyer copies of all pleadings, motions, notices, statements, schedules, applications, reports and other papers filed in Sellers' chapter 11 cases relating to this Agreement or the transactions contemplated hereby.

(d) Operation in the Ordinary Course. Prior to the Closing Date, Sellers shall operate in the Ordinary Course of Business, subject to changes resulting from its chapter 11 cases and the requirements of the Bankruptcy Code and the Bankruptcy Court, and in compliance with all Laws. In furtherance of and without limiting the foregoing, (x) Sellers shall:

(i) maintain and preserve all of the physical Acquired Assets in the same condition as of the date hereof, ordinary wear and tear excepted; and

(ii) perform all of their obligations under the Assigned Contracts, provided, that, except as otherwise required hereunder, Sellers shall not be required to pay any Cure Amounts; and

(iii) maintain insurance at presently existing levels so long as such insurance is available on commercially reasonable terms.

and (y) Sellers shall not, without the prior written consent of Buyer, sell, transfer, mortgage, encumber or otherwise dispose of any of the Acquired Assets other than in the Ordinary Course of Business, execute any Contract other than in the Ordinary Course of Business or agree to or make any commitment to take any actions prohibited by this Section 9(e).

(e) Confidentiality. Prior to the Closing and thereafter, except to the extent required by applicable law (including the Bankruptcy Code) or court order, Buyer and each Seller shall keep strictly confidential all documents and other communications and information whether written or oral, provided by the other prior to or after execution of this Agreement.

(f) Collection of Accounts Receivable. If, following the Closing, Sellers shall collect any Accounts Receivable belonging to Buyer, Sellers shall hold the same in trust and shall promptly pay the same over to Buyer.

(g) Collective Bargaining Agreement. Sellers shall continue to negotiate towards an initial collective bargaining agreement with the labor union known as Paper, Allied-Industrial, Chemical and Energy International Union, AFL-CIO-CLC ("P.A.C.E."), an affiliate of the American Federation of Labor - Congress of Industrial Organizations, and Sellers shall keep Buyer informed of its progress with respect to such negotiations and obtain Buyer's prior written consent prior to executing such agreement.

(h) Continuing Due Diligence Update. On February 6 and 14, 2002, Buyer shall provide Sellers with an oral update on the status of its Continuing Due Diligence. If, in its sole discretion, Buyer determines that it has become aware of information that will result in a termination of this Agreement pursuant to Section 12(a)(iii), Buyer shall so inform Sellers at the February 6th or 14th update, as the case may be; provided, however, that the failure to so inform Sellers shall not result in any liability on the part of Buyer or affect any of its rights hereunder, including its rights under Section 12(b).

10. CONDITIONS TO BUYER'S OBLIGATION TO EFFECT CLOSING

The obligation of Buyer to effect the Closing shall be subject to the satisfaction, on or before the Closing Date, of the following conditions, any one or more of which may be waived by Buyer:

(a) Representations and Warranties and Covenants. (i) The representations and warranties of Sellers set forth in this Agreement shall be true and correct in all material respects as of the date of this Agreement and as of the Closing Date, (ii) Sellers shall have performed and complied in all material respects with the agreements contained in this Agreement required to be performed and complied with by Sellers on or before the Closing, and (iii) each Seller shall have delivered to Buyer at the Closing certificates, dated the Closing Date, signed by their Chief Executive Officer, the President or any Vice President certifying as to compliance with clauses (i) and (ii) above.

(b) Sale Hearing. Sellers shall have obtained the Procedures Order from the Bankruptcy Court by no later than January 22, 2002 scheduling the Sale Hearing to occur by no later than March 6, 2002 and scheduling the Auction to occur not more than two Business Days before the Sale Hearing.

(c) Effectiveness of Sale Order. The Bankruptcy Court shall have entered the Sale Order, 10 days shall have elapsed since such Sale Order was entered (provided, that if the tenth day after such Sale Order is entered is not a Business Day, such period shall be deemed to

have elapsed on the first Business Day following such tenth day), and the effectiveness of such Sale Order shall not have been stayed or, if stayed, such stay shall no longer be in effect.

(d) No Material Adverse Change. From September 30, 2001 until the Closing Date, no Material Adverse Change shall have occurred.

(e) No Litigation. There shall not be any Order, litigation, action or proceeding pending or threatened to be brought before any Governmental Authority seeking to enjoin, restrain or prohibit the transactions contemplated hereby or which, individually or in the aggregate, can reasonably be expected to result in a Material Adverse Change.

(f) Compliance With Procedures Order; Notice. Seller shall have complied with all requirements of the Procedures Order, including the notice requirements provided therein.

(g) Assumption and Rejection of Contracts. The Contracts designated hereunder for assumption or rejection shall be so assumed or rejected, as the case may be, by final Order of the Bankruptcy Court satisfactory to Buyer.

(h) Paper Corp. of the United States. The contract between Paper Corp. of the United States (with which SCI has a supply relationship) and the Bureau of Engraving and Printing shall not have been terminated and shall remain in full force and effect.

(i) Permits. Seller shall have all Permits required by any Governmental Authority to own and operate the Acquired Assets in connection with the Business and such Permits shall be valid and enforceable.

(j) Buyer Financing. The Buyer Financing shall have been funded by the DIP Lenders in accordance with the terms of the Buyer Financing documents and/or commitment letters referred to in Section 12(a)(ix) hereof.

(k) Management Agreements. No member of Sellers' management who has executed a Management Agreement shall have disavowed, canceled or threatened to disavow or cancel such Management Agreement.

(l) xpedx Contract. Sellers shall have obtained an order of the Bankruptcy Court prior to the Closing Date approving the proposed contract between xpedx and SCI pursuant to Section 363(b) of the Bankruptcy Code and payment of the prepetition claims of xpedx pursuant to Section 105(a) of the Bankruptcy Code, in a manner substantially consistent with the motion dated December 21, 2001 now on file with the Bankruptcy Court.

11. CONDITIONS TO SELLERS' OBLIGATION TO EFFECT CLOSING

The obligation of Sellers to effect the Closing shall be subject to the satisfaction, on or before the Closing Date, of the following conditions, any one or more of which may be waived by Sellers:

(a) Representations and Warranties. (i) The representations and warranties of Buyer set forth in this Agreement shall be true and correct in all material respects as of the date of this Agreement and as of the Closing Date, (ii) Buyer shall have performed and complied in all material respects with the agreements contained in this Agreement required to be performed and complied with by Buyer on or before the Closing, and (iii) Buyer shall have delivered to Sellers at the Closing certificates, dated the Closing Date, signed by the sole member of Buyer certifying as to compliance with clauses (i) and (ii) above.

(b) Effectiveness of Sale Order. The Bankruptcy Court shall have entered the Sale Order, 10 days shall have elapsed since the Sale Order was entered (provided, that if the tenth day after the Sale Order is entered is not a Business Day, such period shall be deemed to have elapsed on the first Business Day following such tenth day), and the effectiveness of the Sale Order shall not have been stayed or, if stayed, such stay shall no longer be in effect.

(c) No Litigation. There shall not be any Order, litigation, action or proceeding pending or threatened in writing to be brought before any Governmental Authority seeking to enjoin, restrain or prohibit the transactions contemplated hereby.

12. TERMINATION; EFFECT OF TERMINATION

(a) Termination. This Agreement may be terminated before the Closing occurs only as follows:

(i) By Buyer or by Sellers, if the Closing shall not have occurred for any reason on or before March 27, 2002.

(ii) By Buyer, if one or more of the conditions specified in Section 10 is not satisfied on the Closing Date or such a condition is not reasonably likely to be satisfied prior to the Closing Date.

(iii) By Buyer, by written notice to Sellers on or prior to the Due Diligence Termination Date if Buyer shall not have completed accounting, legal and environmental due diligence concerning Sellers, the Acquired Assets and the Business, including the information contained on the schedules attached hereto, and obtained results satisfactory to it as determined by Buyer in its sole discretion, or Buyer shall have obtained any information showing that the due diligence information previously provided to Buyer by Sellers (including, without limitation, financial projections) is incorrect or incomplete in any material respect or, with respect to financial projections, that there is a material risk that such projections will not be achieved, as determined by Buyer in its sole discretion.

(iv) By Sellers, if one or more of the conditions specified in Section 11 is not satisfied on the Closing Date or such a condition is not reasonably likely to be satisfied prior to the Closing Date.

(v) By Buyer, if (x) the Procedures Order has not been entered by January 22, 2002, (y) the Sale Order has not been entered by March 6, 2002, or if, prior to such date, the Bankruptcy Court approves another transaction involving the sale

or other transfer of any of the Acquired Assets to a third party or (z) Buyer is not the winning bidder in the Auction held by March 4, 2002.

(vi) By Buyer, if the Estimated Net Working Capital exceeds the Target Net Working Capital by an amount greater than \$350,000, unless Sellers waive in writing their right to the Interim Working Capital Adjustment and the Final Working Capital Adjustment.

(vii) By Sellers, if the Target Net Working Capital exceeds the Estimated Net Working Capital by an amount greater than \$350,000, unless Buyer waives in writing its rights to the Interim Working Capital Adjustment and the Final Working Capital Adjustment.

(viii) By Buyer or Sellers, upon an Initial Deposit Repayment.

(ix) By Buyers, by written notice to Sellers on or prior to February 18, 2002, if (x) Buyer shall not have received a binding commitment for the Buyer Financing in form and substance satisfactory to Buyer in its sole discretion or (y) Buyer shall not have entered into Management Agreements satisfactory to Buyer in its sole discretion.

(x) By the mutual written agreement of Buyer and Sellers.

(b) Transaction Expenses. Subject to the following sentence, Sellers shall reimburse Buyer for all reasonable and documented out-of-pocket expenses (including, without limitation, the reasonable fees and expenses of Buyer's professionals) incurred by Buyer in connection with the preparation and negotiation of this Agreement, the Letter of Intent, all documents to be prepared in connection with the consummation of the transactions contemplated by this Agreement (whether consummated or not), and all of Buyer's other fees and expenses related to the transactions contemplated by this Agreement including, but not limited to, Buyer's due diligence and fees and expenses related to the Buyer Financing; provided, however, that in no event shall the aggregate amount of such reimbursement exceed \$300,000 (the "Expense Reimbursement"). The Expense Reimbursement shall constitute an allowed administrative expense claim against Sellers under sections 503 and 507(a) of the Bankruptcy Code, payable, without limitation, from the proceeds of an Alternative Transaction (as defined below) or the assets of Sellers, if and when:

(i) this Agreement terminates for any reason other than a material breach by Buyer of this Agreement;

(ii) Sellers materially breach any of their obligations under this Agreement; or

(iii) Sellers seek approval of, or the Bankruptcy Court approves, any agreement or transaction with a third party for the sale or transfer of all or any portion of the Acquired Assets, directly or indirectly, whether pursuant to a chapter 11 plan for Sellers or under section 363(b) of the Bankruptcy Code, or otherwise enters into

any transaction that is materially inconsistent with this Agreement (an "Alternative Transaction").

(c) Termination Fee. Sellers shall be required to pay Buyer a termination fee in an amount equal to (x) 3% of the Purchase Price minus (y) the actual amount of the Expense Reimbursement (the "Termination Fee") upon the consummation of an Alternative Transaction, which obligation shall constitute an allowed administrative expense claim against Sellers under sections 503 and 507(a) of the Bankruptcy Code, payable from the proceeds of an Alternative Transaction; provided, however, that Buyer shall not be entitled to the Termination Fee if Buyer shall have breached its obligations under this Agreement in any material respect or shall have terminated this Agreement pursuant to Section 12(a)(iii), (viii) or (ix).

(d) Deposit. If the Closing does not occur or this Agreement is terminated, the Deposit shall be paid in accordance with the Escrow Agreement.

(e) No Further Liability. Subject to Sections 12(b), (c) and (d) hereof, if this Agreement is terminated by either or both of Sellers and Buyer pursuant to this Section 12, neither party shall have any further obligation or liability under this Agreement, except that the obligations under Section 9(e) shall survive and any party that has materially breached this Agreement shall not be relieved of any liability hereunder; provided, however, that in the event that, as a result of a breach of this Agreement by Buyer, this Agreement is terminated by Sellers or the Closing does not occur, Sellers shall be entitled, as their sole and exclusive remedy, to liquidated damages as set forth in Section 3(e).

### 13. EMPLOYEES

It is Buyer's intention, subject to the due diligence, to make offers of employment to all employees employed by Sellers in connection with the operation of the Business as of the Closing Date. On or prior to the Closing Date, Buyer and Sellers shall give notice to such employees that they will no longer be employees of Sellers, effective as of the Closing Date, and that Buyer is offering such employees employment at compensation similar to their then present salary and wage rates; provided, that nothing herein shall limit the Buyer's right to terminate any such employee or to modify salaries or wage rates following the Closing Date (any employee who commences employment with the Buyer in connection with the transactions contemplated by this Agreement shall hereinafter be referred to as a "Continuing Employee"). Buyer shall cause Continuing Employees to be credited under any "employee benefit plans" (within the meaning of Section 3(3) of ERISA) established by Buyer or to be established by Buyer for employees of the Business generally with months and years of service which they had been credited under Sellers' plan(s) as of the Closing Date, provided, that such service shall only be recognized for purposes of determining eligibility and vesting under such plans and not for benefit accruals or any other purpose.

### 14. SURVIVAL OF REPRESENTATIONS AND WARRANTIES; INDEMNIFICATION

(a) Survival of Representations and Warranties. The representations and warranties of Sellers and Buyer made pursuant to this Agreement shall survive until 90 days following the Closing Date (the "Survival Termination Date").



(b) Indemnification by Sellers. Sellers shall indemnify and hold harmless Buyer, and shall reimburse Buyer for, any Loss arising from or in connection with (i) any breach of any of the representations and warranties of Sellers in this Agreement or in any certificate delivered by Sellers pursuant to this Agreement, or any actions, omissions or state of facts inconsistent with any such representation or warranty, (ii) any failure by Sellers to perform or comply with any agreement or covenant in this Agreement, and (iii) any liabilities or obligations of Sellers which are not Assumed Obligations. The aggregate liability of Sellers for any such claims under clause (i) shall be limited to, and payable only out of, amounts held under the Post-Closing Escrow Agreement and shall be payable only as and to the extent provided therein. In addition, Buyer shall not be entitled to indemnification by Sellers under Section 14(b)(i) with respect to any claims until the aggregate Loss suffered by Buyer arising from or in connection with all such claims exceeds \$75,000, whereupon Buyer shall be entitled to indemnification hereunder for the amount of such Loss including amounts below \$75,000.

(c) Indemnification by Buyer. Buyer shall indemnify and hold harmless Sellers and shall reimburse Sellers for, any Loss arising from or in connection with (i) any breach of any of the representations and warranties of Buyer in this Agreement or in any certificate delivered by Buyer pursuant to this Agreement, or any actions, omissions or state of facts inconsistent with any such representation or warranty, (ii) any failure by Buyer to perform or comply with any agreement or covenant in this Agreement, and (iii) the Assumed Obligations. Sellers shall not be entitled to indemnification by Buyer under Section 14(c)(i) with respect to any claims until the aggregate Loss suffered by Sellers arising from or in connection with all such claims exceeds \$75,000, whereupon Sellers shall be entitled to indemnification hereunder for the amount of such Loss including amounts below \$75,000.

(d) Procedure for Indemnification with Respect to Direct Claims.

(i) In the event that Buyer shall have a claim for indemnification by Sellers pursuant to Section 14(b)(i), Buyer shall have until the Survival Termination Date to make such claim against Seller.

(ii) Buyer shall make any claim for indemnification by Sellers under this Section 14 by sending to Sellers and the Post-Closing Escrow Agent a written notice specifying the nature of the claim and the dollar amount of Loss incurred by Buyer for which indemnification is sought. The Post-Closing Escrow Agent shall pay to Buyer in accordance with the Post-Closing Escrow Agreement the amount of the Loss if and to the extent that such amount is determined to be payable in accordance with the Post-Closing Escrow Agreement.

(iii) In the event that Sellers shall have a claim for indemnification by Buyer pursuant to Section 14(c)(i), Seller shall have until the Survival Termination Date to make such claim against Buyer by sending Buyer a written notice specifying the nature of the claim and the dollar amount of loss incurred by Sellers for which indemnification is sought.

(e) Procedure for Indemnification with respect to Third Party Claims. Promptly after receipt by an indemnified party under Section 14(b) or (c) of notice of the

commencement or assertion of any action or proceeding, demand or claim (each an "Action"), such indemnified party shall, if a claim in respect thereof is to be made against an indemnifying party under such section, give notice to the indemnifying party of the commencement or assertion thereof, but the failure so to notify the indemnifying party shall not relieve the indemnifying party of any liability that it may have to any indemnified party except to the extent the indemnifying party is prejudiced thereby. In case any such Action shall be brought or asserted against an indemnified party and it shall give notice to the indemnifying party of the commencement or assertion thereof, the indemnifying party shall be entitled to participate therein and, at its election, to assume the defense thereof with counsel reasonably satisfactory to such indemnified party and, after notice from the indemnifying party to such indemnified party of its election so to assume the defense thereof, the indemnifying party shall not be liable to such indemnified party under such section for any fees of other counsel or any other expenses, in each case subsequently incurred by such indemnified party in connection with the defense thereof, other than reasonable costs of investigation, provided, that any indemnified party may, at its own expense, retain separate counsel to participate in any defense at its own expense. Notwithstanding the foregoing, in any Action in which both the indemnifying party, on the one hand, and the indemnified party, on the other hand, are, or are reasonably likely to become, a party, the indemnified party shall have the right to employ separate counsel and to control its own defense of such Action if, in the reasonable opinion of counsel to the indemnified party, either (x) one or more defenses are available to the indemnified party that are not available to the indemnifying party or (y) a conflict or potential conflict exists between the indemnifying party, on the one hand, and such indemnified party, on the other hand, that would make such separate representation advisable, and in such case shall reimburse the indemnified party for the fees and expenses of such counsel. If an indemnifying party assumes the defense of such an Action, (a) no compromise or settlement thereof may be effected by the indemnifying party without the indemnified party's consent unless (i) there is no finding or admission of any violation of law or any violation of the rights of any Person by the indemnified party and (ii) the sole relief provided is monetary damages that are paid in full by the indemnifying party and (b) the indemnifying party shall have no liability with respect to any compromise or settlement thereof effected without its consent. Notwithstanding the foregoing, if an indemnified party determines in good faith that there is a reasonable probability that an Action may adversely affect it or its affiliates other than as a result of monetary damages or if the indemnifying party does not, within ten days after the indemnified party's notice is given, give notice to the indemnified party of its election to assume the defense thereof, such indemnified party may, by notice to the indemnifying party, assume the exclusive right to defend, compromise or settle such Action, provided, that the indemnifying party shall not be bound by (i) any compromise or settlement thereof unless the indemnifying party has given its prior written consent to such compromise or settlement or (ii) any determination of an Action so defended.

15. JURISDICTION

The parties agree that the Bankruptcy Court shall retain jurisdiction to resolve any controversy or claim arising out of or relating to this Agreement, or the breach hereof.

(a) Notices. All notices, requests, demands, consents and other communications required or permitted under this Agreement shall be in writing and shall be considered to have been duly given when (i) delivered by hand, (ii) sent by telecopier (with receipt confirmed), provided that a copy is mailed (on the same date) by certified or registered mail, return receipt requested, postage prepaid, or (iii) received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may from time to time designate as to itself by notice similarly given to the other party in accordance herewith). A notice of change of address shall not be deemed given until received by the addressee.

If to Buyer, to it at:

c/o WR CAPITAL PARTNERS, LLC  
330 South Street  
Morristown, NJ 07962  
Fax No.: (973) 993-2915  
Attention: Jeffrey R. Walsh

with a copy to:

Paul, Weiss, Rifkind, Wharton & Garrison  
1285 Avenue of the Americas  
New York, NY 10019  
Fax No.: (212) 373-2825  
Attention: Robert D. Drain, Esq. and  
Kenneth M. Schneider, Esq.

If to Sellers, to them at:

c/o SPINNAKER INDUSTRIES, INC.  
518 East Water Street  
Troy, OH 45373  
Fax No.: (973) 335-2843  
(203) 972-9372  
Attention: Louis A. Guzzetti, Jr., Chairman and CEO

with a copy to:

Kaye Scholer LLP  
311 South Wacker Drive, Suite 6200  
Chicago, Illinois 60606  
Fax No.: (312) 583-2360  
Attention: Michael B. Solow, Esq.  
Harold D. Israel, Esq.

(b) Press Releases; Disclosure. The parties hereto will cooperate in the issuance of any press releases or otherwise in making any public statements with respect to this Agreement and the transactions contemplated hereby. Neither Buyer nor any Seller shall issue any press release regarding this Agreement or the transactions contemplated hereby without the other party's prior written consent, which consent shall not be unreasonably withheld. Buyer acknowledges and agrees that Sellers may provide copies of this Agreement and the schedules and exhibits attached hereto to the parties in interest in Sellers' chapter 11 cases, and those parties Sellers determine it is necessary to provide copies to in connection with the Auction or as otherwise necessary in connection with Sellers' chapter 11 cases. Sellers also shall be entitled to file copies of this Agreement and the schedules and exhibits attached hereto with the Bankruptcy Court or as otherwise required by law and shall publish notice of this Agreement and the transactions contemplated hereby in the Wall Street Journal or other similar publication.

(c) Definition of Knowledge. As used in this Agreement, with respect to a particular fact or other matter, the phrase "to the knowledge of Sellers," "to the best knowledge of Sellers," "to Sellers' knowledge" or "to Sellers' best knowledge" and any similar phrase shall mean the actual knowledge as of the date of this Agreement of Louis A. Guzzetti, Jr., George E. Fuehrer, Mark J. Wagner, Arthur W. Smith III, Perry J. Schiller, and Kevin W. Ahlfeld.

(d) Entire Agreement. This Agreement and the instruments, agreements, exhibits and other documents contemplated hereby supersede all prior discussions and agreements between the parties with respect to the matters contained herein (including, without limitation, the Letter of Intent, but excluding the Confidentiality Agreement between Buyer and Sellers dated October 25, 2001, which shall remain in full force and effect), and this Agreement and the instruments, agreements and other documents contemplated hereby contain the entire agreement between the parties hereto with respect to the transactions contemplated hereby.

(e) Further Assurances. After the Closing, each of the parties hereto shall hereafter, at the reasonable request of the other party hereto, execute and deliver such other instruments of transfer or assumption and further documents and agreements, and do such further acts and things as may be necessary to carry out the provisions of this Agreement.

(f) Waiver. Any term or condition of this Agreement may be waived at any time by the party thereto which is entitled to the benefit thereof, but such waiver shall only be effective if evidenced by a writing signed by such party. A waiver on one occasion shall not be deemed to be a waiver of the same of any other breach on a future occasion.

(g) Amendment. Except as otherwise expressly provided herein, this Agreement may be amended only by a writing signed by all the parties hereto.

(h) Counterparts. This Agreement may be executed in any number of counterparts, each of which shall be deemed an original and all of which together shall constitute one and the same instrument.

(i) Binding Agreement; Assignment; No Third Party Beneficiaries. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors and permitted assigns. This Agreement may not be assigned by any party

hereto, without the prior written consent of the other party. Any purported assignment without such consent shall be void. Notwithstanding the foregoing, Buyer may, by written notice delivered to Sellers not less than five Business Days prior to the Closing Date, designate one of its affiliates to assume all of the obligations and rights of Buyer hereunder effective as of the Closing Date in a writing reasonably satisfactory to Sellers; upon the effectiveness of such assignment, SC Acquisition, LLC shall be released from liability hereunder. This Agreement is not made for the benefit of any third party (including any non-Seller parties to the Assigned Contracts), and no third party shall be deemed to be a beneficiary hereof.

(j) Governing Law. This Agreement shall be governed by the laws of the State of New York, without regard to the conflicts of laws principles thereof.

(k) Headings. The headings in this Agreement are for convenience of reference only and should not be deemed a part of this Agreement.

(l) Expenses. Except as otherwise expressly provided herein, each of the parties hereto shall pay their own fees and expenses in connection with the negotiation, preparation, execution and delivery of this Agreement and the other instruments and agreements entered into pursuant to this Agreement, and any amendments to the same.

(m) Liability of Members, Officers, Directors of Buyer. No member, officer, or director of Buyer shall have any liability whatsoever for the obligations of Buyer under this Agreement.

[Signatures on Next Page]

IN WITNESS WHEREOF, the parties have caused this Agreement to be duly executed on the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING-MAINE, INC.

By: \_\_\_\_\_  
Name:  
Title:

BUYER:

SP ACQUISITION, LLC

By: \_\_\_\_\_  
Name:  
Title:

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ASSET PURCHASE AGREEMENT

AMENDMENT NO. 1

THIS AMENDMENT NO. 1 (this "Amendment") to the ASSET PURCHASE AGREEMENT, dated of January 18, 2002 (the "Asset Purchase Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and SP Acquisition, LLC (the "Buyer") is made as of February 15, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

WHEREAS, the Sellers and the Buyer wish to modify the Asset Purchase Agreement to extend the date on which the Buyer is entitled to terminate the Asset Purchase Agreement for failure to obtain a binding commitment for Buyer Financing or failure to enter into Management Agreements satisfactory to the Buyer in its sole discretion;

NOW, THEREFORE, the Asset Purchase Agreement is hereby amended as follows:

1. Section 12(a)(ix). Section 12(a)(ix) is hereby deleted and amended to read in its entirety as follows:

"(ix) By Buyer, by written notice to Sellers on or prior to February 25, 2002, if (x) Buyer shall not have received a binding commitment for the Buyer Financing in form and substance satisfactory to Buyer in its sole discretion or (y) Buyer shall not have entered into Management Agreements satisfactory to Buyer in its sole discretion."

2. Ratification of the Asset Purchase Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Asset Purchase Agreement are ratified and shall remain unchanged and continue in full force and effect.

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING-MAINE, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

BUYER:

SP ACQUISTION, LLC

By: \_\_\_\_\_

Name:  
Title:

SPINNAKER COATING, INC.

By: \_\_\_\_\_

Name:  
Title:

SPINNAKER COATING-MAINE, INC.

By: \_\_\_\_\_

Name:  
Title:

BUYER:

SP ACQUISITION, LLC

By: /s/ JEFFREY R. WALSH  
\_\_\_\_\_

Name: JEFFREY R. WALSH  
Title: President

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ASSET PURCHASE AGREEMENT

AMENDMENT NO. 2

THIS AMENDMENT NO. 2 (this "Amendment") to the ASSET PURCHASE AGREEMENT, dated as of January 18, 2002 (the "Asset Purchase Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and SP Acquisition, LLC (the "Buyer") is made as of February 25, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

WHEREAS, the Sellers and the Buyer wish to modify the Asset Purchase Agreement to extend the date on which the Buyer is entitled to terminate the Asset Purchase Agreement if it has not completed its due diligence;

NOW, THEREFORE, the Asset Purchase Agreement is hereby amended as follows:

1. Section 1. The definition of Due Diligence Termination Date in Section 1 is hereby deleted and amended to read in its entirety as follows:

"Due Diligence Termination Date" shall mean February 26, 2002."

2. Ratification of the Asset Purchase Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Asset Purchase Agreement are ratified and shall remain unchanged and continue in full force and effect.

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING-MAINE, INC.

By: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

BUYER:

SP ACQUISITION, LLC

By:

-----  
Name:  
Title:

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING-MAINE, INC.

By: \_\_\_\_\_  
Name:  
Title:

BUYER:

SP ACQUISITION, LLC

By: /s/ JEFFREY R. WALSH  
\_\_\_\_\_  
Name: JEFFREY R. WALSH  
Title: President

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ASSET PURCHASE AGREEMENT

AMENDMENT NO. 3

THIS AMENDMENT NO. 3 (this "Amendment") to the ASSET PURCHASE AGREEMENT, dated as of January 18, 2002 (the "Asset Purchase Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and SP Acquisition, LLC (the "Buyer") is made as of March 5, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

WHEREAS, Sellers and Buyer wish to modify the Asset Purchase Agreement as set forth below;

NOW, THEREFORE, the Asset Purchase Agreement is hereby amended as follows:

1. Section 2(b). Section 2(b) is hereby amended to add the following subsection (xii) to the list of Excluded Assets:

(xii) Preference and avoidance actions or claims under Sections 544, 547 or 548 of the Bankruptcy Code.

2. Section 3(b). Section 3(b) is hereby deleted and amended to read in its entirety as follows:

(b) Closing Payments. At the Closing, pursuant to the terms of the Escrow Agreement, in accordance with instructions of Buyer, the Escrow Agent shall pay (the "Closing Cash Payment") (i) to Sellers, by wire transfer to such bank account(s) designated in writing by Sellers, an amount equal to the Deposit minus the Holdback Amount, (ii) to Buyer, by wire transfer to such bank account(s) designated in writing by Buyer, all earnings on the Deposit and (iii) to the Post-Closing Escrow Agent, in accordance with the terms of the Escrow Agreement substantially in the form attached hereto as Exhibit C, with such changes as shall be required by the Escrow Agent (the "Post-Closing Escrow Agreement"), the Holdback Amount. If this Agreement is terminated after payment of the Deposit for any reason whatsoever, the Deposit and any interest earned thereon (minus \$1,250,000 in the event that Sellers are entitled to liquidated damages as described in Section 3(e)) shall be returned to Buyer within one (1) Business Day of demand by Buyer to the Escrow Agent.

3. Section 3(d). Section 3(d) is hereby deleted in its entirety.

4. Schedule 3(d)(i). Schedule 3(d)(i) is hereby deleted in its entirety.

5. Section 3(e). Each reference to "\$500,000" in Section 3(e) is hereby amended to read "\$1,250,000."

6. Section 9(a). The second sentence of Section 9(a) is hereby deleted in its entirety.

7. Sections 12(a)(vi) and 12(a)(vii). Sections 12(a)(vi) and 12(a)(vii) are hereby deleted in their entirety.

8. Return to Buyer of \$626,000. Sellers and Buyer shall execute and deliver to the Escrow Agent immediately after the execution and delivery of this Amendment an irrevocable instruction to the Escrow Agent in the form attached hereto as Exhibit 1 directing the Escrow Agent to return \$626,000 in immediately available funds to Buyer.

9. Deposit. The term "Deposit" as used in the Asset Purchase Agreement shall hereby mean an amount equal to (i) the sum the Initial Deposit and the Subsequent Deposit reduced by (ii) the amount distributed to Buyer pursuant to Section 8 of this Amendment.

10. Ratification of the Asset Purchase Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Asset Purchase Agreement are ratified and shall remain unchanged and continue in full force and effect.

[Remainder of page intentionally left blank.]

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING-MAINE, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

BUYER:

SP ACQUISITION, LLC

BY: -----

Name:  
Title:

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING-MAINE, INC.

By: \_\_\_\_\_  
Name:  
Title:

BUYER:

SP ACQUISITION, LLC

By: /s/ JEFFREY R. WALSH  
\_\_\_\_\_  
Name: JEFFREY R. WALSH  
Title: President

Ms. Laurel Melody-Casasanta  
State Street Bank and Trust Company  
C/o State Street Bank and Trust Company of Connecticut, N.A.  
Goodwin Square  
225 Asylum Street  
Hartford, Connecticut 06103-0177

Dear Ms. Melody-Casasanta:

Reference is hereby made to that Escrow Agreement, dated as of January 22, 2002 (the "Escrow Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers"), SP Acquisition, LLC (the "Buyer"), and State Street Bank and Trust Company (the "Escrow Agent"). Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to such terms in the Escrow Agreement.

Sellers and Buyer hereby irrevocably instruct Escrow Agent to immediately deliver to Buyer, by wire transfer of immediately available funds to an account designated by Buyer, a portion of the Escrowed Amount equal to \$626,000.

Very truly yours,

SPINNAKER INDUSTRIES, INC.

BY: \_\_\_\_\_

Name:  
Title:

SPINNAKER COATING, INC.

BY: \_\_\_\_\_

Name:  
Title:

SPINNAKER COATING-MAINE, INC.

BY: \_\_\_\_\_

Name:  
Title:

SP ACQUISITION, LLC

BY: \_\_\_\_\_

Name:  
Title:

ESCROW AGREEMENT

AMENDMENT NO. 1

THIS AMENDMENT NO. 1 (this "Amendment") to the ESCROW AGREEMENT, dated as of January 22, 2002 (the "Escrow Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers"), SP Acquisition, LLC (the "Buyer"), and State Street Bank and Trust Company (the "Escrow Agent") is made as of March 5, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Escrow Agreement.

WHEREAS, the Sellers, the Buyer and the Escrow Agent wish to modify the Escrow Agreement to amend provisions related to the distribution of the Escrowed Amount in accordance with amendments made to the Purchase Agreement;

NOW, THEREFORE, the Escrow Agreement is hereby amended as follows:

1. Section 3. Section 3 is hereby deleted in its entirety.

2. Section 4(b). Section 4(b) is hereby deleted and amended to read in its entirety as follows:

(b) If Escrow Agent receives written notice from Buyer and Sellers that the closing (the "Closing") under the Purchase Agreement is consummated, upon written instructions from Buyer, Escrow Agent shall (i) transfer Five Hundred Thousand Dollars (\$500,000) of the Escrowed Amount into the escrow account to be administered by it as escrow agent pursuant to the escrow agreement to be entered into at the Closing among the parties hereto, (ii) deliver an amount equal to the earnings on the Escrowed Amount to Buyer and (iii) deliver the remainder of the Escrowed Amount to Sellers at the Closing by certified or bank cashier's check or by wire transfer pursuant to the direction of Sellers.

3. Sections 4(c) and 4(d). Each reference to "\$500,000" or "Five Hundred Thousand Dollars" in Section 4(c) and Section 4(d) is hereby amended to read "\$1,250,000" and "One Million Two Hundred Fifty Thousand Dollars," respectively.

4. Escrowed Amount. The term "Escrowed Amount" as used in the Escrow Agreement shall hereby mean an amount equal to (i) the sum of (x) the Initial Escrowed Amount and the Subsequent Escrowed Amount minus (ii) \$626,000.

5. Ratification of the Escrow Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Escrow Agreement are ratified and shall remain unchanged and continue in full force and effect.

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING-MAINE, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.  
-----

Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

BUYER:

SP ACQUISITION, LLC

BY: /s/ JEFFREY R. WALSH  
-----

Name: JEFFREY R. WALSH  
Title: President



ESCROW AGENT

STATE STREET BANK AND TRUST  
COMPANY, AS ESCROW AGENT

BY: /s/ LAUREL MELODY-CASASANTA

-----  
Name: LAUREL MELODY-CASASANTA  
Title: Assistant Vice  
President

Ms. Laurel Melody-Casasanta  
State Street Bank and Trust Company  
C/o State Street Bank and Trust Company of Connecticut, N.A.  
Goodwin Square  
225 Asylum Street  
Hartford, Connecticut 06103-0177

Dear Ms. Melody-Casasanta:

Reference is hereby made to that Escrow Agreement, dated as of January 22, 2002 (the "Escrow Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers"), SP Acquisition, LLC (the "Buyer"), and State Street Bank and Trust Company (the "Escrow Agent"). Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to such terms in the Escrow Agreement.

Sellers and Buyer hereby irrevocably instruct Escrow Agent to immediately deliver to Buyer, by wire transfer of immediately available funds to an account designated by Buyer, a portion of the Escrowed Amount equal to \$626,000.

Very truly yours,

SPINNAKER INDUSTRIES, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING, INC.

BY: /s/ LOUIS A. GUZZETTI, JR.

-----  
Name: LOUIS A. GUZZETTI, JR.  
Title: Chairman

SPINNAKER COATING-MAINE, INC.

BY: /s/ Louis A. Guzzetti, Jr.

-----  
Name: Louis A. Guzzetti, Jr.  
Title: Chairman

SP ACQUISITION, LLC

BY: /s/ Jeffrey R. Walsh

-----  
Name: Jeffrey R. Walsh  
Title: President

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ASSET PURCHASE AGREEMENT

AMENDMENT NO. 4

THIS AMENDMENT NO. 4 (this "Amendment") to the ASSET PURCHASE AGREEMENT, dated as of January 18, 2002 (the "Asset Purchase Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and SP Acquisition, LLC (the "Buyer") is made as of March 8, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

WHEREAS, Sellers and Buyer wish to modify the Asset Purchase Agreement as set forth below;

NOW, THEREFORE, the Asset Purchase Agreement is hereby amended as follows:

1. Section 2(b)(xii). Section 2(b)(xii) is hereby deleted and amended and to read in its entirety as follows:

(xii) Preference and avoidance actions or claims under Sections 542, 544, 545, 547, 548, 549 or 550 of the Bankruptcy Code.

2. Ratification of the Asset Purchase Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Asset Purchase Agreement are ratified and shall remain unchanged and continue in full force and effect.

[Remainder of page intentionally left blank.]

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

SPINNAKER COATING, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

SPINNAKER COATING-MAINE, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

BUYER:

SP ACQUISITION, LLC

By: /s/  
-----  
Name:  
Title:

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ASSET PURCHASE AGREEMENT

AMENDMENT NO. 5

THIS AMENDMENT NO. 5 (this "Amendment") to the ASSET PURCHASE AGREEMENT, dated as of January 18, 2002 (the "Asset Purchase Agreement"), by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc. Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and SP Acquisition, LLC (the "Buyer") is made as of March 18, 2002, by and among the Sellers and the Buyer. All capitalized terms used but not defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

WHEREAS, Sellers and Buyer wish to modify the Asset Purchase Agreement as set forth below;

NOW, THEREFORE, the Asset Purchase Agreement is hereby amended as follows:

1. Section 5(b). Section 5(b) is hereby deleted and amended and to read in its entirety as follows:

(b) Closing. If the Sale Order has been entered and has become final, then, subject to the satisfaction or waiver by the parties of the conditions to their respective obligations to effect the Closing set forth in Sections 10 and 11, the Closing shall take place at the offices of Paul, Weiss, Rifkind, Wharton & Garrison at 10:00 a.m. (New York time) on March 28, 2002.

2. Section 12(a)(i). Section 12(a)(i) is hereby deleted and amended and to read in its entirety as follows:

(i) By Buyer or Sellers, if the Closing shall not have occurred for any reason on or before April 5, 2002.

3. Ratification of the Asset Purchase Agreement. Except as otherwise expressly provided herein, all of the terms and conditions of the Asset Purchase Agreement are ratified and shall remain unchanged and continue in full force and effect.

[Reminder of page intentionally left blank.]



\ IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

SPINNAKER COATING, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

SPINNAKER COATING-MAINE, INC.

By: /s/ LOUIS A. GUZZETTI, JR.  
-----  
Name: LOUIS A. GUZZETTI, JR.  
Title:

BUYER:

SP ACQUISITION, LLC

By: -----  
Name:  
Title:

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

SELLERS:

SPINNAKER INDUSTRIES, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING, INC.

By: \_\_\_\_\_  
Name:  
Title:

SPINNAKER COATING-MAINE, INC.

By: \_\_\_\_\_  
Name:  
Title:

BUYER:

SP ACQUISITION, LLC

By: /s/  
\_\_\_\_\_  
Name:  
Title:

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SCHEDULES  
TO  
ASSET PURCHASE AGREEMENT  
DATED JANUARY 18, 2002  
BY AND AMONG  
SPINNAKER INDUSTRIES, INC.,  
SPINNAKER COATING, INC.,  
SPINNAKER COATING-MAINE, INC.  
AND  
SP ACQUISITION, LLC

Unless otherwise indicated, the terms used herein have the meanings given to them in the Asset Purchase Agreement.

Inclusion of an item in these Schedules or delivery of a document pursuant to these Schedules or the Asset Purchase Agreement is not an admission of materiality with respect to the item or document.

Titles of Schedules used herein are for reference only and are not in lieu of their respective definitions in the Asset Purchase Agreement. Although information set forth in these Schedules specifically refers to the paragraph of the Asset Purchase Agreement to which such information is responsive, such information shall be deemed to have been disclosed with respect to any other paragraph of the Asset Purchase Agreement to the extent that such information in its context, without more, would clearly put the Buyer on notice of an exception to a representation or warranty set forth in such other paragraph of the Asset Purchase Agreement.

TRANSAMERICA ENCUMBRANCES

<TABLE>

<S>

Spinnaker Industries, Inc	<C>	<C>
Spinnaker Coating, Inc.	Transamerica Business Credit Corporation,	Blanket Lien
Spinnaker Coating-Maine	as Agent	
	9399 W. Higgins Rd.	
	Rosemont, IL 60018	

</TABLE>

TRANSAMERICA ENCUMBRANCES RELATING TO REAL ESTATE

1. Open-End Mortgage, Assignment of Rents and Security Agreement for Brown-Bridge Industries, Inc. nka Spinnaker Coating, Inc., successor by merger, to Transamerica Business Credit Corporation, dated October 27, 1999, filed for record November 1, 1999 at 2:52:32 PM and recorded in Volume 1108, Page 124, Miami County, Ohio Records to secure the original principal amount of \$3,135,000.00.
2. Financing Statement No. 57629 showing Spinnaker Coating, Inc., as debtor, and Transamerica Business Credit, as secured party, filed August 18, 1999 in Office of Recorder of Miami County, Ohio.
3. Financing Statement No. 57681 showing Spinnaker Coating, Inc., as debtor, and Transamerica Business Credit Corporation, as Agent, as secured party, filed August 30, 1999 in Office of Recorder of Miami County, Ohio.
4. 31. UCC-1 Financing Statement No. U-0058064 showing Spinnaker Coating, Inc., as Debtor, and Transamerica Business Credit Corporation, as Agent, as Secured Party, filed in Miami County, Ohio on November 1, 1999 at 2:55:11 PM.

PERMITTED ENCUMBRANCES

<TABLE>

<CAPTION>

DEBTOR

-----

<S>

Spinnaker Coating, Inc.

SECURED PARTY

-----

<C>

Pace Local 1-1069  
c/o Jonathan S.R. Beal, Esq.  
482 Congress Street  
Portland, ME 04101

COLLATERAL DESCRIPTION

-----

<C>

Assets of SCMI located in Maine.  
(State of Maine Superior Court  
Civil Action  
Order Approving Second Motion  
for Attachment and Trustee  
Process - \$118,500)

Spinnaker Coating, Inc

Tennant Financial Services  
4333 Edgewood Rd.  
Cedar Rapids, IA 52441

Equipment

Spinnaker Coating, Inc

Crown Credit Company  
40 S. Washington St.  
New Bremen, OH 45869

Equipment and Lift Truck

Spinnaker Coating, Inc.

Leasing One Corporation  
P.O. Box 309  
Frankfurt, KY 40602

Equipment

Spinnaker Coating, Inc

Hewlett-Packard Company  
Finance & remarketing Division  
20 Perimeter Summit Blvd.  
Atlanta, GA 30319

Equipment

</TABLE>

PERMITTED ENCUMBRANCES RELATING TO REAL ESTATE

1. Taxes and assessments for the tax year 2002, which are a lien, but not yet due or payable and subsequent years.
2. Title to that portion of the property within the bounds of any roads or highways.
3. Any inaccuracy in the specific quantity of acreage contained on any survey, if any, or contained within the legal description of premises insured herein.
4. Easement rights retained by the public utility and/or railroads, pursuant to Ohio Revised Code Section 723.041.

- 5. Right of way and easement for water line granted to the City of Troy, Ohio by instrument dated April 7, 1971, filed April 26, 1971 at 2:50 PM and recorded in Deed Book 480, Page 80 (As to Inlot 7827).
- 6. Sewer easement granted to the City of Troy, Ohio, by instrument dated July 21, 1939, filed July 24, 1939 at 11:20 AM and recorded in Miscellaneous Record 6, Page 106 (As to Inlot 7827).
- 7. Right of way and easement for the transmission and/or distribution of electric energy, including underground facilities, if any, granted to The Dayton Power and Light Company by instrument dated March 31, 1981, filed April 30, 1981 at 11:03 AM and recorded in Deed Book 556, Page 413 (as to Inlot 6892).
- 8. Easement for the construction, operation, maintenance, repair, replacement, or removal of water, sewer, gas, electric, or other utility line or services and for the express privilege of removing any and all trees or other obstructions to the free use of said utilities and for providing of ingress and egress to the property for said purposes as shown on the plat of Miami County Industries Park-Section 2 as recorded in Plat Book "12", Page 137 (As to Inlot 6892).
- 9. Building restriction line of 30 feet from Marybill Drive as shown on the recorded plat of Miami County Industrial Park-Section 2 as recorded in Plat Book "12", Page 137 and Miami County Industrial Park-Section 3 as recorded in Plat Book "13", Page 137 (As to Inlots 6892 and 7112).
- 10. Reservation of easements for utility installation and maintenance (and drainage) affecting the Westerly (rear) 20 feet, Southerly 10 feet and Easterly 10 feet of caption premises, as shown on the recorded plat of Miami County Industrial Park-Section 2 as recorded in Plat Book "12", Page 137 (As to Inlot 6892).

Drainage Note: The City of Troy does not accept for maintenance any unpaved areas within any open storm drainage easements shown on this plat, and is not obligated to maintain or repair any unpaved channels or slopes in said easements. The easement area of each lot and all improvements in it, excepting concreted or paved areas as required by City of Troy standards, shall be maintained continuously by the owner of the Lot. Within these easements no structure, planting, fencing, culvert or other materials shall be placed or permitted to remain which may obstruct, retard, or change direction of water flow through the drainage channel in the easement.

NOTE: Building, gravel, asphalt paving and concrete dock and wire fence on the insured premises encroaches on said easements as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999.

- 11. Reservation of easements for utility installation and maintenance (and drainage) affecting the Westerly (rear) 20 feet, Northerly 10 feet and Easterly 10 feet of caption premises, as shown on the recorded plat of Miami County Industrial Park-Section 3 as recorded in Plat Book "13", Page 137 (As to Inlot 7112).

Drainage Note: Same as No. 11 above.

NOTE: Fence on the insured premises encroaches on said easement as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999.

- 12. Restrictions contained on the recorded plat of Miami County Industrial Park-Section 3 as recorded in Plat Book 13, Page 137 of Miami County records are as follows: "The Restrictive Covenants and Development Standards for this development shall be the same as shown on Miami County Industrial Park-Section 1, which is filed in Miami County Recorder's Record of Plat Book 12, Pages 48 and 48A (As to Inlot 7112).
- 13. Restrictions appearing of record in Deed Book 605, Page 890 (As to Inlot 7112).
- 14. Possible easement for Electric Tower as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).
- 15. Encroachment by Concrete/waste water pretreatment aeration tank upon premises adjacent to the North as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).
- 16. Possible easement for Overhead Electric affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).
- 17. Easement for Storm Drain pursuant to ORC 723.041 affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).
- 18. Easement for water main pursuant to ORC 723.041 affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).
- 19. Possible easement for Sanitary Sewer affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 7827).



20. Encroachment by wrought iron fence appurtenant to insured premises onto property adjoining on the South as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 330).
21. Encroachment by sign post appurtenant to insured premises onto Marybill Drive as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 6892).
22. Possible easement for electric and telephone affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlot 6892).
23. Encroachment of wire fence by property adjoining on the west affecting insured premises as shown on Plat of Survey by Henry L. Toedtman, Ohio Registered Surveyor No. 7937 (Shaw, Weiss & DeNaples Job No. S4155) dated September 17, 1999 (As to Inlots 6892 and 7112).
24. Financing Statement No. 52672 showing Brown-Bridge Industries, Inc., as debtor, and First Capital Leasing, as secured party, filed September 25, 1997 in Office of Recorder of Miami County, Ohio.
25. Financing Statement No. 55890 showing Spinnaker Coating, Inc., as debtor, and Crown Credit Company as secured party, filed December 1, 1998 in Office of Recorder of Miami County, Ohio.
26. Financing Statement No. 56233 showing Spinnaker Coating, Inc., as debtor, and Crown Credit Company as secured party, filed January 15, 1999 in Office of Recorder of Miami County, Ohio.
27. Financing Statement No. 57073 showing Spinnaker Coating, Inc., as debtor, and Hewlett-Packard Company Finance & Remarketing Division, as secured party, filed May 27, 1999 in Office of Recorder of Miami County, Ohio.

DESCRIPTION OF OTHER ACQUIRED ASSETS

SPINNAKER COATING, INC. (TROY, OHIO)

Real Property Located in Troy

Plant 1: 518 East Water Street, Troy, Ohio, 45373  
Plant 2: 130 Mary-bill, Troy, Ohio 45373

Personal Property

Petty Cash  
Cash in Bank Accounts  
Apartment Deposit  
Deposit with Ohio Bureau of Workers Compensation  
Trade Accounts Receivable  
Miscellaneous Receivables  
All Rights to That Certain Agreement Dated August 3, 1999 By and  
Between Ivex

Packaging Corporation and SCI

All Patents listed on Schedule 7(h) hereof  
Furniture, Fixtures, Office and Lab Equipment  
Machinery & Equipment, Computer Hardware & Software  
All Inventory, No Matter Where Located  
Benefits of Prepaid Expenses  
Educational Loans Receivable  
Trade Name

SPINNAKER COATING-MAINE, INC.

Real Property

None

Personal Property

Cash in Bank Accounts  
Dental Claims Deposits  
Trade Accounts Receivable  
All Rights Under that Certain Asset Purchase Agreement Dated May 14  
2001 By and Among Avery Dennison Corporation, SCMI and SCI  
Furniture, Fixtures, Machinery and Equipment  
All Inventory, No Matter Where Located  
Trade Name

SPINNAKER INDUSTRIES, INC.

Real Property

None

Personal Property

Cash in Bank Accounts  
Benefit of Prepaid Insurance  
Trade Name

SPINNAKER ELECTRICAL TAPE COMPANY

Personal Property

Trade Name

ALLOCATION OF PURCHASE PRICE  
In accordance with Section 3(c).

TARGET STATEMENT OF NET WORKING CAPITAL  
AS OF FEBRUARY 28, 2002

CURRENT ASSETS

<TABLE>

<S>

	<C>	<C>
Accounts Receivable (net)	\$12,547,000	
Inventory (net)	14,351,000	
Prepaid and Other Current Assets	65,000	
	-----	
Total Current Assets		\$26,963,000

CURRENT LIABILITIES

Accounts Payable	\$ 4,400,000	
Accrued Liabilities	3,461,000	
Working Capital Revolver	15,902,000	
	-----	
Total Current Liabilities		\$23,763,000

Target Net Working Capital \$ 3,200,000

</TABLE>

ASSUMED PREPETITION LIABILITIES RELATED TO CUSTOMER CLAIMS  
AND REBATES, TAXES AND EMPLOYEE BENEFITS TO THE EXTENT  
APPROVED BY THE COURT AND NOT SATISFIED BEFORE CLOSING

Liability	Amount Assumed
Accrued Customer Claims & Rebates	\$ 955,000
Accrued Real Estate and Personal Property Taxes	103,000
Accrued Employee Benefits	1,535,000
	-----
Total	\$ 2,593,000
	=====

ADDITIONAL PRE-PETITION LIABILITIES

<TABLE>

<S>

Liability	<C> Amount Assumed
Utilities	\$ 350,000
xpedx	850,000
Freight	350,000
Critical Vendor Contracts	425,000
Reclamation Claims	500,000
	-----
Total	\$ 2,475,000
	=====

</TABLE>

CONFLICTS/CONSENTS: SELLERS

None.



EXECUTORY CONTRACTS; ASSIGNED CONTRACTS

AT&T Suite 1800 1 First National Plaza Dayton, OH 45402	Service Agreement - Webhosting Purchaser
AT&T Suite 1800 1 First National Plaza Dayton, OH 45402	Service Agreement - Internet Access Purchaser
AT&T Suite 1800 1 First National Plaza Dayton, OH 45402	Service Agreement - 1-800 Numbers Purchaser
AT&T Suite 1800 1 First National Plaza Dayton, OH 45402	Service Agreement - VPN Access Purchaser
Ahlfeld, Kevin W. 518 East Water Street Troy, OH 45373	Employment Contract Employer
Ahlfeld, Kevin W. 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Ahlfeld, Kevin W. 518 East Water Street Troy, OH 45373	Special Compensation Agreement Employer
Beigie, Christopher 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Bode Finn 3480 Spring Grove Avenue Cincinnati, OH 45223	Commercial Lease Agreement - Industrial Trash Compactor, Located at Plant 2 (Lease is Capitalized) Lessee
Brennan, Joseph 518 East Water Street Troy, OH 45373	Special Compensation Agreement Employer
Caldabaugh, Karl C. 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Catanzaro, Vincent A. 518 East Water Street Troy, OH 45373	Employment Agreement Employer

Citicapital Commercial Corp.  
P.O. Box 410587  
Kansas City, MO 64141-0587

Lift Truck Lease - Model #GC25HP,  
LP, S/N 4EM91758  
Lift Truck Lease - Model #GC25HP,  
LP, S/N GC254EM91891 Lift Truck Lease -  
Model #GC25HP, LP, S/N GC254EM91890  
Lift Truck Lease - Model #GC24HP, S/N  
4EM92010 Lift Truck Lease - Model  
#GC25HP, S/N 4EM92001 Lessee

Converters Express, Inc.  
18808 142nd Avenue, N.E.  
Building B - Suite 1  
Woodinville, WA 68072

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Crown Credit Company  
P.O. Box 640352  
Cincinnati, OH 45264-0352

Lift Truck Lease - Crown  
RR5020-45TT-240 Lift Truck, S/N  
1A2202304  
Lessee

Drotleff, Andrew  
518 East Water Street  
Troy, OH 45373

Commission Agreement  
Employer

Dunsirn Industries  
9292 9th Street  
Rancho Cucamonga, CA 91730

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
318 Griffith Rd.  
Chicopee, MA 01022

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
13715 Mt. Andersen Street  
Reno, NV 89506

Service Contract -Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
200 Citation Court  
Greensboro, NC 27409

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
2415 Industrial Drive  
Neenah, WI 54956

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Enterprise Fleet Services  
8200 John Carpenter Freeway  
Dallas, TX 75247

Company Fleet Lease - Plant #1 Van,  
1987 Ford Van, Unit #627907  
Company Fleet Lease - Joe Brennan,  
1997 Buick LeSabre, Unit #GJ2183  
Company Fleet Lease - Plant #2 Car,  
1992 Ford Taurus, Unit #G27889 Company  
Fleet Lease - Maria Carson, 1997 Chevy  
Lumina, Unit #GE0112 Company Fleet  
Lease - Andy Drotleff, 1999 Pontiac  
Grand Prix, Unit #GJ4361 Company Fleet  
Lease - Plant #1 Company Car, 1999 Ford  
Taurus, Unit #GJ4436 Company Fleet  
Lease - Barry Jones, 2000 Chevy Impala,  
Unit #GL7668 Company Fleet Lease - Mark  
Mudgett, 2000 Ford Taurus, Unit #GQ7837  
Company Fleet Lease - Mark Mudron, 2001  
Pontiac Grand Prix, Unit #GQ7858  
Company Fleet Lease - Vince McMullin,  
2001 Pontiac Grand Prix, Unit #GQ7861  
Company Fleet Lease - Phil Brotzman,  
2000 Dodge Intrepid, Unit #GQ7936  
Company Fleet Lease - Keith McNair,  
2001 Pontiac Grand Prix, Unit #GQ8125  
Company Fleet Lease - Shawn Paul, 2001  
Dodge Intrepid, Unit #GV4451 Lessee

Enterprise Fleet Services  
8200 John Carpenter Freeway  
Dallas, TX 75247

Service Agreement - Maintenance and  
Tire Management for Enterprise Fleet  
Purchaser.

General Electric Silicones  
Building 80  
260 Hudson River Rd.  
Waterford, NY 12188

Purchase Agreement - Silicones for  
#20 Coater @ Plant 2.  
Purchaser

Genuity Solutions  
P.O. Box 101337  
Atlanta, GA 30392-1337

Service Agreement - Webhosting and  
Internet Access (To Be Replaced With  
AT&T Agreements)  
Purchaser

P.H. Glatfelter Company  
Corporate Headquarters  
Spring Grove, PA 17362

Rebate Program - Rebates on Postage  
Materials, Flourescents and Label Mat  
Purchaser

Gomez, Debra S.  
518 East Water Street  
Troy, OH 45373

Employment Contract  
Employer

Gustafson, David 518 East Water Street Troy, OH 45373	Employment Contract Employer
Gustafson, David 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Hewlett-Packard Company Finance & Remarketing Division 20 Perimeter Summit Blvd. Atlanta, GA 30319	Operating Lease - Network Server Lessee
Interstate Gas Supply P.O. Box 20456 Columbus, OH 43220	Purchase Agreement - Natural Gas Purchasing Agreement Purchaser
Jones, Barry 518 East Water Street Troy, OH 45373	Commission Agreement Employer
Merritt, Cindy 518 East Water Street Troy, OH 45373	Special Compensation Agreement Employer
Montco, Inc. 556 Columbia Drive Carrollton, GA 30117	Service Contract - Third Party Slitting and Distribution Purchaser
P.I.C. Industries, Inc. 1851 Dawns Way Fullerton, CA 92631	Service Contract - Third Party Slitting and Distribution Purchaser
Pagell Corporation 74 Lowland Street Holliston, MA 01746	Service Contract - Third Party Slitting and Distribution Purchaser
Pitney Bowes 1 Kohnle Drive Miamisburg, OH 45342	Contract - Postage Machine Purchaser
Pressure Sensitive Materials, Inc. D.B.A. Presscut 13725 Maine Street Lemont, IL 60439	Service Contract - Third Party slitting and Distribution Purchaser
QAD Inc. 10,000 Mid-Atlantic Drive Suite 200 East Mt. Laurel, NJ 08054	Maintenance Agreement - QAD Software Purchaser
Riley, Brad 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Schiller, Perry J. 518 East Water Street Troy, OH 45373	Employment Contract Employer
Schiller, Perry J. 518 East Water Street Troy, OH 45373	Severance Agreement Employer
Schiller, Perry J. 518 East Water Street Troy, OH 45373	Special Compensation Agreement Employer
Smith III, Arthur W. 518 East Water Street Troy, OH 45373	Employment Contract Employer

Smith III, Arthur W.  
518 East Water Street  
Troy, OH 45373

Severance Agreement  
Employer

Smith III, Arthur W.  
518 East Water Street  
Troy, OH 45373

Special Compensation Agreement  
Employer

Solutia Inc.  
500 Park Boulevard  
Suite 500  
Itasca, IL 60143-2657

Purchase Agreement - Acrylic  
Emulsions (B-122)  
Purchaser

Verizon Wireless  
FLG-510  
P.O. Box 110  
Tampa, FL 33601

Maintenance Agreement - Cellular  
Phones  
Purchaser

Waco Warehouse  
1250 Archer Drive  
Troy, OH 45373

Operating Lease - Month-to-Month  
Agreement (Inventory Storage, Paid  
Monthly, Based on Volume in  
Inventory)  
Lessee

Wagner, Mark J.  
518 East Water Street  
Troy, OH 45373

Employment Contract  
Employer

Wagner, Mark J.  
518 East Water Street  
Troy, OH 45373

Severance Agreement  
Purchaser

Wagner, Mark J.  
518 East Water Street  
Troy, OH 45373

Special Compensation Agreement  
Employer

Wausau-Mosinee  
515 W. Davenport Street  
Rhineland, WI 54501

Purchase Agreement - 42# and 53#  
Liner  
Purchaser

Wright Express Fleet Fueling  
P.O. Box 390024  
Boston, MA 02241-0924

Contract - Monthly Fueling Contract  
for Leased Vehicles  
Purchaser

Dunsirn Industries  
9292 9th Street  
Rancho Cucamonga, CA 91730

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
318 Griffith Road  
Chicopee, MA 01022

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
13715 Mt. Andersen Street  
Reno, NV 89506

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
200 Citation Ct.  
Greensboro, NC 27409

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Dunsirn Industries  
2415 Industrial Drive  
Neenah, WI 54956

Service Contract - Third Party  
Slitting and Distribution  
Purchaser

Fore River Dist. 217 Read Street Portland, ME 04103	Operating Lease - Month-to-Month Agreement (Inventory Storage, Paid Monthly, Based on Volume in Inventory) Lessee
Land Reclamation, Inc. 84 Warren Avenue Westbrook, ME 04092	Operating Lease - Storage/Warehouse Space (to Expire 12/31/2001) Lessee
M&S Transport, Inc. Route One North Watseka, IL 60970	Service Contract - Third Party Distribution Purchaser
Montco, Inc. 565 Columbia Drive Carrollton, GA 30117	Service Contract - Third Party Slitting and Distribution Purchaser
National Distribution Center, Inc. D.B.A. Vineland Construction Company 905 Avenue T, Suite 312 Grand Prairie, TX 75050	Service Contract - Third Party Distribution Purchaser
Nexus Distribution Corp. 550 Albion Avenue Schaumburg, IL 60193	Service Contract - Third Party Distribution Purchaser
Northland Industrial Truck P.O. Box 845534 Boston, MA 02284-5534	Lift Truck Lease - Yale Lift Truck (S/N B818D03359W) Lift Truck Lease - Yale Lift Truck (S/N E187V09443W) Lift Truck Lease - Yale Lift Truck (S/N E187V09444W) Lessee
Pressure Sensitive Materials, Inc. D.B.A. Presscut 13725 Maine Street Lemont, IL 60439	Service Contract - Third Party Slitting and Distribution Purchaser
Sappi Fine Paper North America 225 Franklin Street Boston, MA 02101	Lease and Purchase Agreement - \$1.00 By-Back
Sandra Reid	Employment Arrangement

AUDITED FINANCIALS  
Previously provided to Buyer.

CURRENT BALANCE SHEET

SPINNAKER COATING, INC. AND SPINNAKER COATING-MAINE, INC.

September 30, 2001  
\$000

Prepared consistently with year end audited financial statements (except with respect to the exclusion of Entoleter, Inc., Spinnaker Industries, Inc. and Spinnaker Electrical Tape Company, which were included in the year end audited financial statements).

Does not consider the effects of the Companies' chapter 11 bankruptcy filing.

<TABLE>  
<CAPTION>

	SEPT. 30, 2001
	-----
<S>	<C>
ASSETS	
Current assets	
Cash and cash equivalents	--
Accounts receivable, net	12,532
Inventories	16,024
Prepaid expenses and other	71
Deferred income taxes	--
	-----
Total current assets	28,627
Property, plant and equipment	
Land	390
Buildings and improvements	5,384
Machinery and equipment	26,375
	-----
	32,149
Accumulated Depreciation	(17,518)
	-----
	14,631
Goodwill, net	659
Investment in subsidiaries	--
Intercompany accounts	4,670
Other assets	390
	-----
Total assets	\$ 48,977
	=====

</TABLE>



CURRENT BALANCE SHEET (CONT'D)  
SPINNAKER COATING, INC. AND SPINNAKER COATING-MAINE, INC.

SEPTEMBER 30, 2001

\$000

<TABLE>

<S>

<C>

Liabilities and stockholders' equity	
Current liabilities	
Accounts payable	\$ 7,145
Accrued liabilities	4,941
Accrued FIT	--
Current portion long term debt	5
Working capital revolver	21,748
Other current liabilities	--
	-----
Total current liabilities	33,839
Long term debt, less current portion	10,104
Notes, 10-3/4%	--
Intercompany	71,830
Deferred income taxes	--
Pension liability and OPEB	1,364
Stockholder's equity	
Common stock	11
Additional paid in capital	7,786
Retained earnings	(75,957)
Minimum pension liability	--
Less: Treasury stock	--
	-----
Total stockholders' equity	(68,160)
	-----
Total liabilities and stockholders' equity	\$ 48,977
	=====

</TABLE>

EQUIPMENT

Note: Does not include equipment of SCMI which Sellers owned as of September 30 and subsequently sold, with all proceeds then used to repay the Working Capital loan.

Equipment:

All signs.

All coating machinery including Coaters 2, 4, 17, 18, 19 and 20.  
All adhesive and silicone storage and delivery systems.  
All drying equipment.

All slitting and rewinding equipment.  
All sheeting and packaging equipment.

All material handling equipment including, but not limited to, conveyors, lift tables and lift trucks.  
All storage racks.  
All tools, operating supplies and spare parts.

All quality control equipment.

All laboratory equipment.

All sprinkler and fire protection systems.  
All heating and air conditioning equipment.  
All pollution control equipment.

All office furniture and equipment including, but not limited to, desks, chairs, tables, copiers, carpeting and displays.

All computer equipment and software including, but not limited to, personal computers, printers, scanners, networking equipment, disk drives, tape drives, docking stations, modems and engineering CAD systems.  
All telephone and other communications equipment.  
All vehicles, including, but not limited to, company cars and trucks.

All other Equipment owned by Sellers necessary or used to operate the Business as it has been operated prior to the date hereof.

INTELLECTUAL PROPERTY

<TABLE> <CAPTION>							
COUNTRY	REFERENCE#	TYPE	FILED	SERIAL#	ISSUED	PATENT#	STATUS
<S> RELEASABLE ADHESIVE SHEET MATERIAL							
	<C>	<C>	<C>	<C>	<C>	<C>	<C>
CANADA	P29727CA0	CEQ	5/23/1984	454,922	12/28/1988	1,247,462	ISSUED
UNITED STATES	P29727US1	CIP	7/1/1985	06/750,827	12/30/1986	4,632,872	ISSUED
UNITED STATES	P29727US2	DIV	6/5/1986	06/871,636	10/6/1987	4,698,248	ISSUED
AN IMPROVED SPLICE							
UNITED STATES	P29728US0	NEW	11/4/1993	08/148,766	12/5/1995	5,472,755	ISSUED

<TABLE> <CAPTION>							
COUNTRY	REFERENCE#	FILED	APPL#	REGDT	REG#	STATUS	CLASSES
<S> BROWN-BRIDGE							
	<C>	<C>	<C>	<C>	<C>	<C>	<C>
United States	T29704US0	8/14/1978	73/181,923	6/23/1981	1,158,085	REGISTERED	17
CLIMATIZED							
CANADA	T29701CA0	4/28/1977	410,113	4/17/1981	257987	REGISTERED	N/A
FLATOUT							
UNITED STATES	T29707US0	9/2/1982	73/383,343	5/17/1983	1,238,344	REGISTERED	

<TABLE>

<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
PANCAKE							
CANADA	T29718CA0	1/31/1969	319,449	8/28/1970	170,814	REGISTERED	N/A
GERMANY	T29721DE0	5/13/1969	B42 316/16 WZ	7/23/1970	871,189	REGISTERED	16
UNITED KINGDOM	T29722GB0	9/25/1968	931,433	5/9/1969	931,433	REGISTERED	16
UNITED STATES	T29708US0	11/16/1967	72/284,988	2/4/1969	864,562	REGISTERED	
PANCAKE PLUS							
AUSTRALIA	T29717AU0	10/11/1982	A 382359	6/5/1986	A382359	REGISTERED	16
UNITED KINGDOM	T29723GB0	2/25/1981	1,149,469	10/18/1984	1,149,469	REGISTERED	16
QUICKETT							
UNITED STATES	T29709US0	7/13/1981	73/318,600	1/11/1983	1,223,405	REGISTERED	
RED STREAK							
UNITED STATES	T29710US0			3/20/1956	623,321		
UNITED STATES	T29971US0	2/23/1998	75/438,928	10/31/2000	2,398,931	REGISTERED	17
SATIN-L							
UNITED STATES	T29711US0	12/21/1979	243,757	8/25/1981	1,166,487	REGISTERED	16
STRIP-RITE							
UNITED STATES	T29712US0	8/25/1977	73/138,876	4/11/1978	1,089,193	REGISTERED	
STRIP-TAC							
UNITED STATES	T29972US0	2/23/1998	75/439,100	12/14/1999	2,299,417	REGISTERED	16

</TABLE>

<TABLE> <S> STRIP-TAC PLUS	<C>	<C>	<C>	<C>	<C>	<C>
UNITED STATES	T29714US0	4/14/1983	73/421,671	5/22/1984	1,278,934	REGISTERED
TANDA-TAC						
UNITED STATES	T29715US0	5/2/1983	73/424,230	5/1/1984	1,276,117	REGISTERED

</TABLE>

MATERIAL SOFTWARE LICENSES

Licensors  
-----

IBM International Passport Agreement  
gad, inc.

Products  
-----

Lotus Notes System  
Information management system

COMPLIANCE WITH LAWS

None.

PERMITS

AIR PERMITS

PLANT #1  
FACILITY SOURCE ID#0855140083

Permit-to-Operate Permits	Expires
-----	-----
#5 Coater	02/05
#2 Coater	02/05

Registration Status Permits	Date Reg.
-----	-----
Safety-Kleen Degreaser	10/29/1991
Tank T-3 (Recovered Toluene)	6/10/1988
Tank T-2 (Methanol)	3/17/1989
Tank T-1 (New Toluene)	3/17/1989
Holding Tank 6A	4/7/1989
Holding Tank 6B	4/7/1989
Coater #4 Emulsion Coating	7/11/1986
Leffel Boiler #4	12/27/1979
Bryan Model L-56 Boiler	12/27/1979
Leffel Boiler #2	12/27/1979
Leffel Boiler #3	12/27/1979

PLANT #2  
FACILITY SOURCE ID#0855140350

Permit-to-Operate Permits	Expires
-----	-----
#20 Coater	12/11/2006

Registration Status Permits	Dates Reg.
-----	-----
#19 Coater, Flexo Printer	10/24/1986
#17 Coater, Hot Melt	11/28/1986

WATER DISCHARGE PERMITS  
PLANT #1

Regulator	Expires
-----	-----
Ohio EPA	01/31/04

PLANT #2 Regulator	Expires
-----	-----
Ohio EPA	Expired

Notes:

-----

1. Currently, Plant #1 is operating its air contaminant sources pursuant to state permits to operate. However, Plant: #1 (Facility 0855140083) made a timely application for a Title V permit. A draft Title V permit and a proposed Title V permit have been issued. Ohio EPA's local air agency -- the Regional Air Pollution Control Agency (RAPCA) -- informed Spinnaker personnel recently that the issuance of the final Title V permit would occur by the end of February 2002. The new Title V permit will be readily transferable to the purchaser of Spinnaker's assets pursuant to the administrative permit amendment provisions in O.A.C. 3745-77.

2. Plant #1 discharges non-contact cooling water and storm water pursuant to NPDES permit No. 11FO0009\*ED/OH0010626. The permit expired on January 31, 1999. However, timely application for its renewal was made by Spinnaker personnel prior to January 31, 1999, and Spinnaker considers the permit to be in force. However, Ohio EPA has not acted upon the application, Spinnaker representatives are communicating with Ohio EPA personnel in the Division of Surface Water to confirm the status of the permit. Spinnaker has continued to comply with all terms and conditions of the permit, including sampling and the submission of discharge monitoring reports.

3. Plant #2 discharges storm water only pursuant to a state general surface water discharge permit. Spinnaker's discharge of storm water was covered under Ohio's general permit through August 2000. On August 1, 2000, Ohio's general permit was renewed by U.S. EPA and a new Notice of Intent (NOI) to be covered under that permit had to be submitted. To date, Spinnaker has not submitted the NOI.

EXCLUDED PERMITS

All operating permits associated with Spinnaker Coating - Maine, Inc.



ENVIRONMENTAL MATTERS

1. In 1994, SCI purchased the assets of the Brown-Bridge operation of Kimberly-Clark Corporation ("K-C"). Prior to closing the transaction, SCI conducted environmental due diligence to evaluate the assets. Due diligence revealed petroleum-based solvent contamination in soil and ground water on the site. K-C covenanted to remediate the soil and ground water contamination after the closing, and began its remedial activities in the spring of 1995. To date, most remedial goals for the contaminants have been achieved, with the exception of ground water remedial goals for vinyl chloride and trichloroethene. Accordingly, K-C continues to pump and treat groundwater pursuant to an administrative order issued by the Director of Ohio EPA in March 2001.
  
2. As part of its 1994 pre-acquisition due diligence, SCI conducted an asbestos survey of the Plant 1 facility. As a result of the survey, SCI and K-C negotiated an arrangement whereby K-C agreed to remove asbestos-containing materials in certain portions of the facility. K-C properly completed that work. Asbestos containing material remains in other locations of the facility, which, to the best of Seller's knowledge, is intact and does not pose a risk to human health.

EMPLOYEE MATTERS

LIST OF EMPLOYEES NOT GOVERNED BY COLLECTIVE BARGAINING AGREEMENTS:

EMPLOYEE -----	DOH ---	JOB TITLE -----
AHLFELD, KEVIN	01/19/98	VICE PRESIDENT MERCH
ALLEN, PHYLLIS	12/15/75	SHIFT MANAGER
BACH, WILLIAM	10/03/94	CREDIT & COL COOR
BAKER, GEORGIA	02/19/79	SR RESEARCH TECH
BAKER, LISA	03/19/79	MARKET SPECIALIST-GO
BEAM, BRIAN	12/01/01	INFO SYSTEMS SPEC
BERGQUIST, ANGELA	06/30/97	INFO SYSTEMS SPEC
BLASZKIEWICZ, BRIAN	08/25/97	PROCESS ENGINEER
BRENNAN, JOSEPH	07/16/01	SR REGIONAL SALES MG
BRESSLER, MICHELLE	01/02/01	BUSINESS DEVELOPMENT
BRICKER, TONI	12/26/84	EXECUTIVE ADMINISTRA
BROOKHART, PAMELIA	07/03/86	ADMINISTRATIVE ASST
BROTZMAN, PHILLIP	02/27/84	FIELD SALES REP
BRUMBAUGH, KAREN	10/23/89	CUSTOMER SERVICE REP
CAMPBELL, RICHARD	11/10/97	SR LAB TECHNICIAN
CARSON, MARIA	02/11/97	REGIONAL SALES MGR
CATANZARO, VINCENT	09/23/96	TECHNICAL MARKETING
CHIEN, WENCHENG	06/30/97	PROGRAMMER ANALYST
COLLETT, ELISE	06/29/76	ORDER ENTRY & INV SP
CORNS, RANDALL	08/30/99	PROCESS ENGINEERING
COTA, PAMALA	11/16/00	PURCHASING ASSISTANT
COVERSTONE, GREGORY	11/21/00	CUSTOMER SERVICE ASS
DAGLEY, JEFFREY	09/18/00	MANAGER, PRODUCTION
DAVIS, J. DARIN	01/15/97	INFORMATION SYSTEMS
DECKER, KATHLEEN	07/01/84	ORDER ENTRY & INV AS
DESZCZ, JOHN	08/14/00	MANAGER, FINANCIAL R
DICKERSON, PAUL	02/18/91	BUSINESS DEV ENGINEE
DROTLEFF, ANDREW	06/28/99	FIELD SALES REP
FELLOWS, BRADFORD	04/03/00	BUYER/PLANNER
FERGUSON, JANA	04/12/99	FINANCIAL ASSISTANT
FIESSINGER, JEFFREY	06/12/95	SHIFT MANAGER
FOSTER, MYRNA	10/26/92	RESEARCH LAB TECH 2
FUEHRER, GEORGE	04/01/01	EXECUTIVE
FURBEE, ALISA	01/05/98	SENIOR RESEARCH LAB
GOMEZ, DEBRA	05/17/99	BENEFITS ADMINISTRAT
GREEN, LARRY	09/10/01	DIR-HUMAN RESOURCES
GREER, BARBARA	04/01/99	COMPLAINT COORDINATO
GUSTAFSON, DAVID	04/18/95	TECHNICAL SERVICE MA
GUZZETTI, LOUIS	04/01/01	EXECUTIVE

HACKETT, KAREN	07/02/90	FINANCIAL ASSISTANT
HAHN, CARL	02/02/78	COATING TEAM LEADER
HARLEMAN, MARK	04/20/98	PLANT 2 FINISHING TE
HARTLEY, PATRICIA	10/17/88	BUYER/PLANNER
HILL, JULIE	08/22/83	CUSTOMER SERVICE REP
HOOPER, ALLEN	01/01/02	MANAGER, PRODUCTION
HOWELL, VICKIE	10/30/78	CUSTOMER SERVICE REP
JAMES, RICHARD	05/21/73	RESEARCH SCIENTIST
JENKINS, HOPE	05/01/00	WAREHOUSE CLERK
JONES, BARRY	04/20/98	FIELD SALES REP
KLENK, RONALD	04/24/91	SENIOR ENVR, HEALTH,
KUHL, VIRGIL	12/17/90	TECHNICAL GROUP LEAD
LANDIS, TIMOTHY	07/06/81	SHIFT MANAGER
LONG, DEANNA	11/20/89	FINANCIAL ASSISTANT
MAGOTO, CYNDA	07/02/90	CUSTOMER SERVICE REP
MALONE, SHARON	03/04/97	MANAGER OF DIST & LO
MANNING, DEBORAH	10/10/77	BUYER/PLANNER
MATTHEWS, MELODY	12/16/01	RECEPTIONIST
MCGLAUGHLIN, KAREN	04/22/85	SENIOR RESEARCH LAB
MCMULLIN, VINCENT	04/08/85	SR FIELD SALES REP
MCNAIR, KEITH	08/21/00	FIELD SALES REP
MERRITT, CINDY	06/05/95	SDC PLANNER
MILLETT, WILLIAM	01/01/02	MAINTENANCE TECHNICI
MONNIN, DANA	10/16/78	ADMINISTRATIVE ASST
MUDGETT, MARK	05/14/01	SENIOR FIELD SALES R
MUDRON, MARK	05/14/01	SENIOR FIELD SALES R
OTTE, DENISE	07/16/79	FINANCIAL COORDINATO
PARR, GEORGE	09/19/88	SENIOR PROJECT ENGIN
PAUL, SHAWN	06/18/01	FIELD SALES REP
PHILLABAUM, DAVE	06/24/96	INFO SYSTEMS SPEC
POSTLE, STUART	01/02/79	PLANT 2 COATING MANA
POUDER, DUANE	05/20/96	SENIOR PLANNER
RATLIFF, MIRIAM	01/18/88	MARKETING ASSISTANT
RAWE, ROGER	08/31/81	FINANCIAL COORDINATO
REED, SANDRA	12/23/96	DIRECTOR QA/ANALYTIC
RIDER, LEE	03/06/00	SR. TECH SRVC SPEC
RILEY, BRAD	03/18/96	DIRECTOR OF BUSINESS
ROSE, BECKY	11/15/99	RESEARCH LAB TECH I
SCHILLER, PERRY	04/25/00	VICE PRESIDENT FINAN
SEVER, MELANIE	12/30/96	FINANCIAL ANALYST
SHAFFER, ROBERT	06/19/68	SHIFT MANAGER
SHARP, MARY	08/01/88	SDC/FREIGHT MANAGEME
SHELLHAAS, JOHN	04/15/85	COMMODITY MANAGER
SMITH, ARTHUR	10/09/95	VICE PRESIDENT SUPPL
STORMS, WILLIAM	04/09/91	QUALITY ASSUR MANAGE
SWARTZ, JEFFREY	11/13/00	SHIFT MANAGER
THORNE, DEBORAH	03/11/96	CUSTOMER SERVICE REP

UNGER, A. JEAN	07/01/88	CREDIT & COL ASSISTA
VOILES, JUDITH	06/06/01	CUSTOMER SERVICE ASS
WAGNER, MARK	06/25/96	VP INFORMATION & QUA
WARD, BECKY	12/27/94	PROD REPORTING CLERK
WOLFE, CAROLYN	07/01/81	MANAGER, TELEPHONE S
BAKER, LORINDA	09/05/01	BUSINESS ANALYST
LIPTAK, DEBORAH	05/11/99	CUSTOMER SERVICE SPE
WELLS, BETTY	08/02/99	PLANT 2 SECRETARY

LIST OF COLLECTIVE BARGAINING AGREEMENTS

See "Reduction-In-Force Agreement with Paper, Allied-Industrial, Chemical & Energy Workers International Union" signed and dated April 13, 2001.

Collective bargaining agreement governing hourly employees is currently being negotiated with Paper, Allied-Industrial, Chemical & Energy Workers International Union.

No further Collective Bargaining Agreements.

LIST OF EMPLOYEE BENEFIT PLANS

<TABLE>  
<CAPTION>

VENDOR -----	BENEFIT -----
<S>	<C>
Aetna U.S. Healthcare	Medical Insurance
Aetna U.S. Healthcare	Dental Insurance
Liberty Mutual	Life Insurance
Liberty Mutual	Accidental, Death & Dismemberment Insurance
Company Administered (self insured)	Short-Term Disability Insurance
Liberty Mutual	Long-Term Disability Insurance
Company Administered (self insured)	Education Assistance Benefit
Human Affairs International (HAI)	
Magellan Behavioral Health Co.	Employee Assistance Program
Standard Insurance Company	401(k) Plan

</TABLE>

ABSENCE OF CERTAIN CHANGES

1. Matters disclosed in pleadings and schedules filed in Sellers' chapter 11 bankruptcy case.
2. Since the commencement of Sellers' chapter 11 bankruptcy case, certain of Sellers' vendors have tightened their credit terms with Sellers.
3. SII was delisted from AMEX effective December 28, 2001, and has filed to terminate registration under the Securities and Exchange Act of 1934.

LIABILITIES

1. Administrative expenses incurred under the Bankruptcy Code solely on account of the Sellers' bankruptcy proceeding.

INSURANCE

<TABLE>  
<CAPTION>

EXPIRATION DATE	INSURANCE TYPE	INSURANCE COVERAGE
-----	-----	-----
<S>	<C>	<C>
01/30/02	General Liability	\$1,000,000
01/31/02	Property	\$129,254,809
01/30/02	Umbrella	\$25,000,000
01/30/02	Auto	\$1,000,000
01/01/02 Ext. to 1/30/02	Crime	\$1,000,000
11/30/02	Worker's Comp. (2)	Statutory
05/15/02	Foreign Liability	\$1,000,000
04/25/02	Fiduciary Liability	\$3,000,000
	Stop Gap Liability (2)	
8/31/2003 (1)	Directors' & Officers' (SKK)	\$10,000,000

</TABLE>

<TABLE>  
<CAPTION>

EXPIRATION DATE	POLICY NUMBER	CARRIER NAME	RENEWAL STATUS
-----	-----	-----	-----
<S>	<C>	<C>	<C>
01/30/02	Y660165J6996TIL01	Travelers	will renew
01/31/02	PTN45-92-78	Royal & Sunalliance	declined to renew
01/30/02	BE7402135	National Union Fire Insurance	will renew
01/30/02	DRE3331700-D31948 - MASS. DRE3331600-D31948 All Others.	United States Fidelity & Guaranty (Enterprise)	will renew
01/01/02 Ext. to 1/30/02	473-97-14	A.I.G.	will renew
11/30/02	ACS350567	Royal & Sunalliance	renewed
05/15/02	PST223767206	CNA Insurance Companies	
04/25/02	008FF10318297	Travelers	
8/31/2003 (1)	169556773	C.N.A. Insurance Companies	

</TABLE>

- (1) Policy period is from 8/31/00 to 8/31/03; premium of 236,500 was paid upfront in 2000 through the Lynch Corporation.
- (2) Spinnaker's Ohio employees are covered under a State of Ohio program for Worker's Comp. For the approximately 12 sales and executive employees outside Ohio the Company purchases Worker's Comp. Insurance with a maximum annual benefit of \$500,000. Beyond the stated limit the Company is self-insured.



TAXES

None.

WARRANTY, PRICING AND OTHER ACCOMMODATIONS

<TABLE>  
<CAPTION>

	2001	2000	1999
<S>	<C>	<C>	<C>
GROSS SALES	\$ 91,348	\$105,433	\$106,172
TOTAL CREDITS ISSUED	2,105	2,659	1,925

Total Credits Issued include all credits issued by SCI for warranty, pricing and other accommodations.

REAL PROPERTY

None.

LITIGATION

A. SCI LITIGATION

<TABLE>  
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Caption of Suit and Case Number	Nature of Proceeding	Court of Agency and Location	Status or Disposition
Thomas May v. Spinnaker Coating Case No. 01-433	Intentional Tort, negligence, punitive damages.	Common Pleas Court of Miami County, Ohio	Pending
AmeriComm Direct Marketing v. Spinnaker Coating	Preference Payment	US Bankruptcy Court, District of Delaware	Not Filed, Verbal Demand Received
Thomas Bricker v. Spinnaker Coating Case No. 00-6	Intentional Tort, negligence	Common Pleas Court of Miami County, Ohio	Settled-last payment of \$125,000.00 due November 5, 2001.
Spinnaker Coating, Inc. v. Troy Laminating and Coating, Inc., Case No. 01-3344	Contract claim	United States Bankruptcy Court, Southern District of Ohio, Dayton Division	Pending

</TABLE>

B. SCMI LITIGATION

<TABLE>  
<CAPTION>

Caption of Suit and Case Number	Nature of Proceeding	Court of Agency and Location	Status or Disposition
Spinnaker Coating Maine v. PACE Local 1-1069 Case No. 01-CV-232-P-H	Company seeks declaratory judgment that Maine severance statute is unconstitutional. Action also seeks order enjoining further prosecution of the action described immediately below.	U.S District Court District of Maine	Pending
PACE Local 1-1069 v. Spinnaker Coating-Maine, Inc. Case No. 01-CV-236-P-H	PACE seeks payment of amounts allegedly owed pursuant to Maine Statute.	U.S. District Ct. District of Maine	Pending
Pace Local 1-1069 AFL-CIO-CLC . (Spinnaker Coating-Maine Inc). Case No. 1-CB-9824-1	Unfair labor practice charge filed by Spinnaker alleging PACE failed to bargain in good faith over severance benefits due after closure of Maine Plant	National Labor Relations Board, Region 1	Pending

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CONFLICTS/CONSENTS: BUYER

None.

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UNITED STATES BANKRUPTCY COURT  
FOR THE SOUTHERN DISTRICT OF OHIO  
WESTERN DIVISION AT DAYTON

IN RE:	)	CASE NO. 01-38066
	)	JOINTLY ADMINISTERED
SPINNAKER INDUSTRIES, INC., ET AL.,	)	
	)	CHAPTER 11
	)	
DEBTORS.	)	JUDGE HOFFMAN

-----

ORDER PURSUANT TO SECTIONS 105, 363, 365 AND 1146 OF  
THE BANKRUPTCY CODE: (A) AUTHORIZING AND APPROVING  
ASSET PURCHASE AGREEMENT WITH NEWCO; (B) AUTHORIZING  
THE SALE OF SUBSTANTIALLY ALL OF THE DEBTORS' ASSETS, FREE  
AND CLEAR OF ALL LIENS, CLAIMS, INTERESTS, CHARGES AND ENCUMBRANCES, SUBJECT  
TO THE TERMS OF THE ASSET PURCHASE AGREEMENT; (C) AUTHORIZING THE DEBTORS TO  
CONSUMMATE ALL TRANSACTIONS RELATED TO THE ABOVE; AND (D) GRANTING OTHER RELIEF

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This matter is before the Court on the motion (the "Motion") dated January 4, 2002 of Spinnaker Industries, Inc. ("Spinnaker") and its wholly owned subsidiaries, as debtors and debtors in possession herein (collectively, the "Debtors"), for the entry of, inter alia, this order (the "Sale Order"): (A) authorizing and approving that certain asset purchase agreement as Amended on March 5, 2002 (the "Asset Purchase Agreement"), a copy of which is attached hereto as Exhibit A, between Spinnaker, Spinnaker Coating, Inc. and Spinnaker Coating-Maine, Inc. (collectively, the "Sellers") and Spinnaker Acquisition, LLC; (B) authorizing the sale of substantially all of the Debtors' assets free and clear of all liens, claims, interests, charges and encumbrances, subject to the terms of the Asset Purchase Agreement and subject to higher and/or better offers (collectively, as described and defined in the Asset Purchase Agreement, the "Acquired Assets"); (C) authorizing the Debtors to consummate all transactions related to the

above; and (D) granting other relief including scheduling auction, approving expense reimbursement and termination fee, and approving bidding procedures; and the Court having on January 22, 2002 entered its Order, inter alia, (i) Scheduling a Hearing to Approve Asset Purchase Agreement with Buyer for the Sale of Substantially All of the Debtors' Assets, Free and Clear of All Liens, Claims, Interests, Charges and Encumbrances, Subject to Higher or Better Offers, (ii) Setting an Auction Date, (iii) Approving Expense Reimbursement Termination Fee, (iv) Approving the Form and Manner of Notice in Connection Therewith, and (v) Approving Bidding Procedures for the Submission of Any Competing Bids (the "Procedures Order"); and the Debtors having received the highest and best bid for the Acquired Assets from SP Acquisition, LLC, a Delaware limited liability company (the "Buyer") pursuant to the Asset Purchase Agreement; and the Court having considered the Motion and the record in these proceedings, and having heard the statements of counsel in support of the relief requested in the Motion at a hearing before the Court on March 5, 2002 (the "Sale Hearing"); and the Court having been fully advised and having determined that the legal and factual bases set forth in the Motion and at the Sale Hearing establish just cause for the relief granted in this Sale Order;

LAW: THE COURT MAKES THE FOLLOWING FINDINGS OF FACT AND CONCLUSIONS OF

JURISDICTION

A. The Court has jurisdiction over this matter under 28 U.S.C. Sections 157 and 1334. This proceeding is a core proceeding under 28 U.S.C. Section 157(b)(2). Venue is proper in this district under 28 U.S.C. Sections 1408 and 1409.

NOTICE

B. The Debtors have complied with all of the procedures for notice of the Motion and Sale Hearing set forth in the Procedures Order. Such notice constitutes appropriate



and adequate notice to all parties and is in compliance with Rules 2002, 6004, 6006 and 9014 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"). No other or further notice of the Motion, the Sale Hearing or the entry of this Sale Order is necessary or required.

OBJECTIONS; AUCTION; AND OTHER BIDDERS

C. In response to the Motion and the notice of the Motion, the Debtors have received objections to the proposed sale of the Acquired Assets to the Buyer under and pursuant to the Asset Purchase Agreement from the following parties: the Official Committee of Unsecured Creditors of Spinnaker Coating, Inc. (the "Committee"), The United States Trustee and the Ohio Environmental Protection Agency. No other objection to the Motion or the proposed sale to the Buyer has been filed with this Court.

D. An auction (the "Auction") was conducted at Coolidge, Wall, Womsley & Lombard, March 4, 2002. The Buyer, Charlesbank Equity Fund V Limited Partnership ("Charlesbank"), the Debtors and the Committee participated at the Auction, which was conducted fairly and openly.

E. On March 5, 2002, the Court conducted the Sale Hearing. Immediately prior to the Sale Hearing, Charlesbank advised the Committee that they were withdrawing from the Auction process. At such time, the Committee concluded that the Buyer's offer was the highest and best offer and withdrew its pending objections to the Motion. The Debtors and the Committee submitted the Buyer's offer to the Court for approval as the highest and best offer for the Acquired Assets.

F. In response to the Motion, the notice of the Motion and the Procedures Order, the Debtors have received no offers to purchase the Acquired Assets higher and/or better than the Buyer's offer. Accordingly, the Buyer's bid is the highest and best bid for the Acquired Assets.

JUSTIFICATION FOR SALE

G. The Debtors have established sound business justification in support of the proposed sale. Such business justifications include, but are not limited to, the fact that (i) an immediate sale will improve the Sellers' prospects to retain important contracts and (ii) the Debtors believe that, as set forth in the Motion, a sale pursuant to section 363 of title 11 of the United States Code (the "Bankruptcy Code") and subject to higher and better offers is the most effective means of maximizing the value for the Acquired Assets. After considering the circumstances described in the Motion, the Court has determined that the procedures outlined in the Procedures Order and the Buyer's offer present the best opportunity for the Debtors to realize the highest recovery possible for the Acquired Assets for the benefit of all creditors. The sale process conducted by the Financial Advisor and the Debtors was non-collusive, fair and reasonable, and conducted in good faith.

H. The transactions contemplated by the Motion, as approved and implemented by this Sale Order, are in compliance with and satisfy all applicable provisions of the Bankruptcy Code, including, without limitation, sections 363(b), (f) and (m) and 365 of title 11 of the United States Code (the "Bankruptcy Code"). The terms and conditions of the sale of the Acquired Assets and the other transactions approved by this Sale Order are fair and reasonable.

I. The Buyer's offer, as approved by this Sale Order, is the highest and best offer for the Acquired Assets. The aggregate purchase price offered by the Buyer constitutes full and adequate consideration and reasonably equivalent value for the Acquired Assets.

J. The transfer of the Acquired Assets at the Closing (as defined in the Asset Purchase Agreement) to the Buyer for the consideration set forth in the Asset Purchase Agreement is in the best interests of the Debtors' estates, their creditors and all parties in interest.

GOOD FAITH

K. The sale process conducted pursuant to the Procedures Order was non-collusive, fair and reasonable, and was conducted openly and in good faith. The transfer of the Acquired Assets to the Buyer represents an arm's-length transaction and has been negotiated in good faith between the parties. The Buyer, as transferee of the Acquired Assets, is a good faith purchaser under section 363(m) and, as such, is entitled to the full protection of section 363(m) of the Bankruptcy Code.

SALE FREE AND CLEAR OF LIENS, CLAIMS AND ENCUMBRANCES

L. The Debtors are authorized to sell the Acquired Assets free and clear of all Liens (as defined in Paragraph 4 hereinafter) pursuant to and in accordance with section 363(f) of the Bankruptcy Code; provided that that this order shall not extinguish any obligations that the Debtors may have to the Ohio Environmental Protection Agency or the United States Environmental Protection Agency under applicable state or federal environmental laws that Debtors, Buyer and any other parties may have regarding the Debtors' Troy property.

LEASES AND CONTRACTS TO BE ASSUMED AND ASSIGNED

M. Upon the transfer of the Assigned Contracts(1) (consisting of certain real property leases and executory contracts) to the Buyer and, subject to the payment of the cure amounts (as set forth in Exhibit B to this Order) contemplated and required by this Sale Order: (A) each Lease constitutes a valid and existing leasehold interest in the property subject to such Lease; (B) none of the Debtors' rights (including options, renewals and extensions) have been released or waived under any of the Assigned Contracts; (C) the Assigned Contracts have not been terminated and are in full force and effect; and (D) no default on the part of the Debtors

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(1) All capitalized terms used herein but not otherwise defined herein shall have the meanings ascribed to such terms in the Asset Purchase Agreement.

(monetary or non-monetary) exists under any Assigned Contract (including, without limitation, with respect to any amounts payable thereunder), nor does there exist any event or condition which with the passage of time or the giving of notice, or both, would constitute such a default.

CORPORATE AUTHORITY; CONSENTS AND APPROVALS

N. The Debtors have full corporate power and authority to execute the Asset Purchase Agreement, any related agreements and all other documents contemplated by the Asset Purchase Agreement or such other related agreements, and the sale of the Acquired Assets by the Debtors has been duly and validly authorized by all necessary corporate power and authority necessary to consummate the transactions contemplated by the Asset Purchase Agreement. No consents or approvals, other than this Sale Order and those expressly provided for in the Asset Purchase Agreement, are required for the Debtors to consummate such transactions.

BASED UPON THE FOREGOING, IT IS HEREBY ORDERED that

1. The Motion is approved.

2. The Asset Purchase Agreement and the terms and conditions contained therein are approved. The Debtors are authorized and directed at the Closing to execute, deliver, implement and fully perform the Asset Purchase Agreement, together with all additional instruments, agreement and documents which are contemplated by the Asset Purchase Agreement and those instruments, agreements and documents which may be reasonably necessary, convenient or desirable in implementing the Asset Purchase Agreement, and to take all further actions (including any prorations, adjustments and the like provided for in the Asset Purchase Agreement) as may be necessary or appropriate in performing the obligations as contemplated by the Asset Purchase Agreement. All objections to the Motion that were not withdrawn or settled on the record or otherwise are overruled.

3. Subject to the fulfillment of the terms and conditions of the Asset Purchase Agreement, at the Closing, the Debtors are authorized to sell, transfer, assign and convey to the Buyer all of the Debtors' rights, title and interest in and to the Acquired Assets. The Debtors are authorized and empowered at the Closing to deliver bills of sale, assignments and such other documentation contemplated by the Asset Purchase Agreement and this Sale Order.

4. Except with respect to any obligations that the Debtors may have to the Ohio Environmental Protection Agency or the United States Environmental Protection Agency under applicable state or federal environmental laws that Debtors, Buyer and any other parties may have regarding the Debtors' Troy property, the transfer of the Acquired Assets to the Buyer as of the Closing will be free and clear of any and all Liens. As used herein, the term "Liens" shall mean (a) any and all mortgages, security interests, conditional sales or other title retention agreements, pledges, liens, claims, judgments, demands and encumbrances, hypothecation, rights of setoff, recoupment or other offset, lis pendens or other charge or interest, and (b) all debts arising under, relating to, or in connection with any acts of the Debtor, claims (as that term is defined in 11 U.S.C. Section 101(5)), obligations, demands, guarantees, options, rights, contractual commitments, restrictions, interests and matters of any kind and nature, in the case of each of clauses (a) and (b), whether imposed by agreement, understanding, statute, law, equity or otherwise, and whether direct or indirect, absolute or contingent, choate or inchoate, fixed or contingent, matured or unmatured, liquidated or unliquidated, and whether arising prior to, on or after the Filing Date (as defined in the Motion), including, without limitation, claims and encumbrances (i) that purport to give any party a right or option to effect any forfeiture, modification, right of first refusal, or termination of any of any Debtor's or the Buyer's interests

in the Acquired Assets, or any similar rights, (ii) relating or arising under or out of, in connection with, or in any way relating to either or both the Acquired Assets or the operation of the Debtors' businesses prior to the Closing, (iii) any taxes of any kind accrued for, applicable to or arising from any period (or portion thereof) ending on or prior to the Closing, and (iv) the liens and claims identified on Exhibit B to the Motion.

5. This Sale Order is and will be effective as a determination that, upon the Closing, all Liens in, on or upon the Acquired Assets are adjudged and declared to be unconditionally released, discharged and terminated, with all such Liens to attach to the cash proceeds of the sale of the Acquired Assets (net of all Cure Amounts as hereinafter defined in paragraph 8(a), the "Proceeds"), with the same force, validity, effect, priority and enforceability, inter se, as such Liens had in the Acquired Assets prior to such sale. Except as otherwise provided in this Sale Order, any issues regarding the extent, validity, perfection, priority and enforceability of such Liens with respect to such proceeds will be determined by the Court, if, as and when appropriate, upon proper application at a later date, including pursuant to a proposed plan of liquidation.

6. The Proceeds shall be distributed as follows:

A. At Closing the Buyer is authorized and directed to remit directly to Transamerica Business Capital Corporation (the "Agent") as agent for Debtors' pre-petition and post-petition Lenders that portion of the Proceeds equal to all of the Obligations then outstanding (as defined in the Final Order (1) Authorizing Debtors-In-Possession To Incur Post-Petition Secured Obligations, (2) Granting Security Interests and Priority Pursuant to 11 U.S.C. 364(c) and (d), (3) Granting Adequate Protection, And (4) Modifying Automatic Stay entered on December 11, 2001 (the "Financing Order" and such cash payment, the "DIP Payment")). Upon

and subject to the Closing, (i) all of the Obligations then owing to the Agent and the Lenders (as defined in the Financing Order) and paid through the DIP Payment shall be deemed allowed as a fully secured claim, and the provisions of Paragraphs J, K and L and clause (i) of the second sentence of Paragraph 25 of the Financing Order shall be binding on all parties in interest, (ii) the Buyer's payment in full in cash of the DIP Payment shall constitute payment in full of an equivalent amount of Indebtedness, and the Debtors and their estates shall have no further liability for such Indebtedness, and the payment of such DIP Payment shall be final and conclusive and binding on all parties in interest and shall not be set aside or otherwise avoided for any reason, and (iii) upon Agent's receipt of the DIP Payment, its Liens on and security interests in the Acquired Assets shall be released.

B. The Proceeds, after payment of the DIP Amount to Agent, shall be maintained by the Debtors and used by the Debtors to administer and wind-down their estates and for distribution in respect of remaining claims and Liens (including the payment of administrative expense claims). The Debtors will deposit the Proceeds in a segregated, interest bearing account and copies of account statements will be provided to the Committee. All Liens (other than the Agent's Liens) shall attach to such Proceeds with the same force, validity, effect, priority and enforceability, inter se, as such Liens had in the Acquired Assets prior to such sale.

7. Notwithstanding anything to the contrary contained herein, this Sale Order shall not, in any way, affect, impair or restrict the Liens, claims, encumbrances and interests of any entity (including the Debtors) in, against, or with respect to, any of the Debtors' assets other than the Acquired Assets.

8. A. The Debtors are authorized to assume the Assigned Contracts and assign them to the Buyer. The Buyer has provided adequate assurance of its future performance

under the Assigned Contracts, and the assumption and assignment of the Assigned Contracts to the Buyer satisfy the requirements of section 365 of the Bankruptcy Code. Notwithstanding any provision of the Assigned Contracts (including those described in sections 365(b)(2) and (f) of the Bankruptcy Code) that prohibits, restricts or conditions an assignment or transfer, the Debtors are authorized and directed at the Closing, pursuant to section 365 of the Bankruptcy Code, to assume the Assigned Contracts and assign their rights, title and interest therein to the Buyer. The amounts set forth on Exhibit B to the Order (the "Cure Amounts") shall constitute the full and final cure and other payments required under section 365(b) and (f) of the Bankruptcy Code to assume and assign to buyer each of the respective Assigned Contracts listed thereon. Except as provided in Section 4 of the Asset Purchase Agreement or as otherwise provided in a written agreement or in the Asset Purchase Agreement, the Debtors are authorized and directed to pay the Cure Amounts to the respective holders of such claims from the proceeds of the sale promptly after the Closing Date.

B. Upon the assignment of the Assigned Contracts and the payment of the Cure Amounts, pursuant to section 365(k) of the Bankruptcy Code, the Debtors shall be relieved from any further liability under the Assigned Contracts.

9. The Rejected Contracts (as defined in the Motion) shall be deemed rejected as of the Closing Date, pursuant to section 365 of the Bankruptcy Code. Each of the Lessors shall be required to file a proof of claim with the Clerk of the Court, on or before April 14, 2002 for any and all alleged damages arising from the rejection of its Rejected Contracts.

10. Except as expressly set forth in this Sale Order or the Asset Purchase Agreement, the Buyer has not, and will not be deemed to have, assumed any Liens including "claims" (as that term is defined in section 101(5) of the Bankruptcy Code) against the Debtors.



11. All of the Debtors' rights, title and/or interests in the Acquired Assets are as of the Closing, transferred to and vested in the Buyer. Subject to the fulfillment of the terms and conditions of the Asset Purchase Agreement, as of the Closing, this Sale Order will be considered and constitute for any and all purposes a full and complete general assignment, conveyance and transfer of the Acquired Assets or a bill of sale transferring good and marketable title in the Acquired Assets to the Buyer. Any and all governmental recording offices and all other parties, persons or entities are authorized to accept this Sale Order as such an assignment or bill of sale and, if necessary, this Sale Order may be accepted for recordation on or after the Closing as conclusive evidence of the free and clear, unencumbered transfer of title to the Acquired Assets conveyed to the Buyer at the Closing.

12. The transfer of the Acquired Assets to the Buyer under this Sale Order is exempt from any transfer or stamp tax under section 1146(c) of the Bankruptcy Code, whether imposed or assessable against the Debtors of the Buyer.

13. If any of the Acquired Assets are in the care or custody of any non-debtor party, such party following the Closing shall immediately, upon written request and presentation of this Sale Order, surrender any such Acquired Assets in its care or custody to the Buyer.

14. Upon the Closing, the Buyer is granted immediate and unfettered access to the Acquired Assets. The Debtors and their officers, agents and employees who have access to and control over any of the Acquired Assets shall cooperate in delivering the Acquired Assets to Buyer and shall cease exercising control over the Acquired Assets upon the Closing, except as directed by the Buyer in accordance with the Asset Purchase Agreement and this Sale Order, and such parties are enjoined after the Closing from exercising any control and/or interfering with the Buyer's use, peaceful enjoyment and control of the Acquired Assets without the Buyer's

consent. Provided, however, that Buyer shall make certain senior management personnel of the Debtors who are under the Buyers' control available to the Debtors and/or the Committee for valid estate purposes for a period not to exceed sixty (60) days after Closing, and such availability shall not exceed five (5) hours per week in the aggregate. The Debtors' estates shall indemnify such senior management personnel for such services and reimburse their reasonable out-of-pocket costs and expenses.

15. Effective on the Closing Date, each of the Debtors' creditors having Liens on any of the Acquired Assets is authorized and directed to execute such documents and take all actions as may be necessary to release its Liens, if any, in, on or against the Acquired Assets, if any, as such Liens may have been recorded or may otherwise exist.

16. Except as provided in the Asset Purchase Agreement, if any person or entity that has filed financing statements or other documents or agreements evidencing Liens in, on or against the Acquired Assets has not delivered to the Debtors prior to the Closing, in proper form for filing and executed by the appropriate parties, termination statements, instruments of satisfaction, releases of all Liens or other interests that such person or entity has with respect to the Acquired Assets, the Debtors and the Buyer are authorized to execute and file such statements, instruments, releases and other documents on behalf of such person or entity with respect to the Acquired Assets.

17. This Court has exclusive jurisdiction to implement and enforce the terms and provisions of the Asset Purchase Agreement (and all documents contemplated thereby) and this Sale Order, including any disputes relating thereto or with respect to the sale, the proceeds of the sale, the transfer or assignment and delivery of the Acquired Assets to the Buyer and the Buyer's peaceful use and enjoyment thereof after the Closing, free and clear of any Liens,

regardless of whether a plan of reorganization has been confirmed in these chapter 11 cases and irrespective of the provisions of any such plan or order confirming such plan; and the Court retains jurisdiction over the parties to the Asset Purchase Agreement with respect to any controversies which may arise thereunder.

18. The terms and provisions of this Sale Order are binding in all respects upon the Debtors, their employees, officers and directors, their creditors, their shareholders, any parties having received notice of these proceedings, any affected third parties and other parties-in-interest, any persons asserting a Lien in, on or against the Acquired Assets, the Buyer and all of the aforementioned parties' successors or assigns, including, without limitation, any trustee subsequently appointed for the Debtors under the Bankruptcy Code.

19. The failure specifically to include any particular provisions of the Asset Purchase Agreement or the agreements contemplated thereby in this Sale Order will not diminish the effectiveness of such provision, it being the intent of this Court that the Asset Purchase Agreement and agreements contemplated thereby are authorized, approved and effective in their entirety. In the event of any inconsistency between this Sale Order and the Asset Purchase Agreement, this Sale Order and the terms hereof shall be controlling.

20. This is a final order and enforceable upon its entry. To the extent necessary under Rules 5003, 6004(g), 6006(d), 9014, 9021 and 9022 of the Bankruptcy Rules, the Court expressly finds that there is no just reason for delay in the implementation of this Sale Order and expressly directs entry of judgment as set forth in this Sale Order. This Sale Order shall be effective immediately and the stay imposed by Bankruptcy Rule 6004(g) is otherwise abrogated.

21. Under section 363(m) of the Bankruptcy Code, the reversal or modification of this Sale Order on appeal will not affect the validity of the transfer of the Acquired Assets to the Buyer, as well as the transactions contemplated or authorized by this Sale Order, unless the same is stayed pending appeal prior to the Closing of the transactions authorized by the Sale Order.

22. Except as otherwise set forth herein or in the Asset Purchase Agreement, under no circumstances shall the Buyer be deemed a successor of or to the Debtors with respect to any Liens of others against or in the Debtors or the Acquired Assets of any kind or nature whatsoever. The sale, transfer, assignment and delivery of the Acquired Assets shall not be subject to any Liens, of any kind or nature whatsoever (other than the obligations under the Assigned Contracts accruing after the Closing Date), which Liens shall remain with, and continue to be obligations of, the Debtors and attach to the Proceeds. All persons holding any Lien, other than the obligations under the Assigned Contracts accruing after the Closing Date, against or in the Debtors or the Acquired Assets of any kind or nature whatsoever shall be, and hereby are, forever barred, estopped, and permanently enjoined from asserting, prosecuting, or otherwise pursuing such Lien of any kind or nature whatsoever against the Buyer, its property, its successors and assigns, or the Acquired Assets with respect to any Lien of any kind or nature whatsoever, other than an obligation under the Assigned Contracts accruing after the Closing Date, such person or entity had, has, or may have against or in the Debtors, their estates, officers, directors, shareholders, or the Acquired Assets. Following the Closing Date, no holder of a Lien against the Debtors shall interfere with the Buyer's title to or use and enjoyment of the Acquired Assets based on or related to such Lien. Other than the obligations under the Assigned Contracts accruing after the Closing Date, under no circumstances shall any holder of a Lien be able to

<PAGE> 15

commence, continue or otherwise pursue or enforce any remedy, claim or cause of action against the Buyer, and each holder of a Lien is permanently enjoined from commencing, continuing or otherwise pursuing or enforcing any remedy, claim or cause of action against the Buyer on account of such Lien.

23. Each non-Debtor party to the Assigned Contracts is hereby forever barred, estopped, and permanently enjoined from asserting against the Buyer or its property any default existing as of the Closing, any counterclaim, defense, setoff or any other claim asserted or assertable (as of the Closing) against the Debtors or the Buyer.

Dated: March \_\_, 2002  
Dayton, Ohio

UNITED STATES BANKRUPTCY JUDGE

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AMENDMENT OF AGREEMENT

Reference is made to an Agreement (the "Agreement") dated as of August 17, 2001 among Lynch Corporation (the "Company"), Ralph R. Papitto ("Mr. Papitto") and Mario J. Gabelli ("Mr. Gabelli").

WHEREAS, the parties to the Agreement wish to amend it to terminate certain of their respective obligations thereunder.

NOW, THEREFORE, in consideration of the premises and the mutual agreements contained herein, the parties agree as follows:

1. Sections 2, 5, 6 and 7 of the Agreement shall be, and they hereby are, deleted therefrom, and the parties shall have no further obligations under or in respect of said Sections 2, 5, 6 and 7. The parties acknowledge and agree that this Amendment terminates the Company's obligation to grant the Option (as defined in Section 2 of the Agreement) which was intended to be granted to Mr. Papitto but which had not been accepted by Mr. Papitto or submitted to the shareholders of the Company for their approval.

2. All other terms and provisions of the Agreement are hereby ratified and confirmed.

IN WITNESS WHEREOF, the parties have signed this Amendment as of this 7th day of February, 2002.

/s/ RALPH R. PAPIITTO  
-----  
RALPH R. PAPIITTO

/s/ MARIO J. GABELLI  
-----  
MARIO J. GABELLI

LYNCH CORPORATION

By: /s/ RAYMOND H. KELLER  
-----  
RAYMOND H. KELLER

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LYNCH CORPORATION  
2001 EQUITY INCENTIVE PLAN

1. PURPOSE

The purpose of this Equity Incentive Plan (the "Plan") is to advance the interests of Lynch Corporation (the "Company") and its subsidiaries by enhancing their ability to attract and retain employees and other persons or entities who are in a position to make significant contributions to the success of the Company and its subsidiaries through ownership of shares of the Company's common stock ("Stock"), and cash incentives.

The Plan is intended to accomplish these goals by enabling the Company to grant Awards in the form of Options, Stock Appreciation Rights, Restricted Stock or Unrestricted Stock Awards, Deferred Stock Awards or Performance Awards, or combinations thereof, all as more fully described below.

2. ADMINISTRATION

Unless otherwise determined by the Board of Directors of the Company (the "Board"), the Plan will be administered by the Company's Executive Compensation and Benefits Committee (the "Committee").

The Committee will have authority, not inconsistent with the express provisions of the Plan and in addition to other authority granted under the Plan, to (a) grant Awards at such time or times as it may choose; (b) determine the size of each Award, including the number of shares of Stock subject to the Award; (c) determine the type or types of each Award; (d) determine the terms and conditions of each Award; (e) waive compliance by a holder of an Award with any obligations to be performed by such holder under an Award and waive any terms or conditions of an Award; (f) amend or cancel an existing Award in whole or in part (and if an award is canceled, grant another Award in its place on such terms and conditions as the Committee shall specify), except that the Committee may not, without the consent of the holder of an Award, take any action under this clause with respect to such Award if such action would adversely affect the rights of such holder; (g) prescribe the form or forms of instruments that are required or deemed appropriate under the Plan, including any written notices and elections required of Participants (as defined below), and change such forms from time to time; (h) adopt, amend and rescind rules and regulations for the administration of the Plan; and (i) interpret the Plan and decide any questions and settle all controversies and disputes that may arise in connection with the Plan. Such determinations and actions of the Committee, and all other determinations and actions of the Committee made or taken under authority granted by any provision of the Plan, will be

conclusive and will bind all parties. Nothing in this paragraph shall be construed as limiting the power of the Committee to make adjustments under Section 7.3 or Section 8.6.

3. EFFECTIVE DATE AND TERM OF PLAN

The Plan will become effective on the date on which it is approved by the stockholders of the Company. Awards may be made prior to such stockholder approval if made subject thereto. No Award may be granted under the Plan after December 10, 2011, but Awards previously granted may extend beyond that date.

4. SHARES SUBJECT TO THE PLAN

Subject to adjustment as provided in Section 8.6, the aggregate number of shares of Stock that may be delivered under the Plan will be 300,000. If any Award requiring exercise by the Participant for delivery of Stock terminates without having been exercised in full, or if any Award payable in Stock or cash is satisfied in cash rather than Stock, the number of shares of Stock as to which such Award was not exercised or for which cash was substituted will be available for future grants.

Subject to Section 8.6(a), the maximum number of shares of Stock as to which Options or Stock Appreciation Rights may be granted to any Participant in any one calendar year is 200,000, which limitation shall be construed and applied consistently with the rules under Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Code").

Stock delivered under the Plan may be either authorized but unissued Stock or previously issued Stock acquired by the Company and held in treasury. No fractional shares of Stock will be delivered under the Plan.

5. ELIGIBILITY AND PARTICIPATION

Each key employee of the Company or any of its subsidiaries (an "Employee") and each other person or entity (including without limitation non-Employee directors of the Company or a subsidiary of the Company) who, in the opinion of the Committee, is in a position to make a significant contribution to the success of the Company or its subsidiaries will be eligible to receive Awards under the Plan (each such Employee, person or entity receiving an Award, "a Participant"). A "subsidiary" for purposes of the Plan will be a corporation in which the Company owns, directly or indirectly, stock possessing 50% or more of the total combined voting power of all classes of stock.

6.1. OPTIONS

(a) Nature of Options. An Option is an Award giving the recipient the right on exercise thereof to purchase Stock.

Both "incentive stock options," as defined in Section 422(b) of the Code (any Option intended to qualify as an incentive stock option being hereinafter referred to as an "ISO"), and Options that are not ISOs, may be granted under the Plan. ISOs shall be awarded only to Employees. An Option awarded under the Plan shall be a non-ISO unless it is expressly designated as an ISO at time of grant.

(b) Exercise Price. The exercise price of an Option will be determined by the Committee subject to the following:

(1) The exercise price of an ISO or an Option intended to qualify as performance based compensation under Section 162(m) of the Code shall not be less than 100% of the fair market value of the Stock subject to the Option, determined as of the time the Option is granted.

(2) In no case may the exercise price paid for Stock which is part of an original issue of authorized Stock be less than the par value per share of the Stock.

(c) Duration of options. The latest date on which an Option may be exercised will be the tenth anniversary of the day immediately preceding the date the Option was granted, or such earlier date as may have been specified by the Committee at the time the Option was granted.

(d) Exercise of Options. An Option will become exercisable at such time or times, and on such conditions, as the Committee may specify. The Committee may at any time and from time to time accelerate the time at which all or any part of the Option may be exercised. Any exercise of an Option must be in writing, signed by the proper person and delivered or mailed to the Company, accompanied by (1) any documents required by the Committee and (2) payment in full in accordance with paragraph (e) below for the number of shares for which the Option is exercised.

(e) Payment for Stock. Stock purchased on exercise of an Option must be paid for as follows: (1) in cash or by check (acceptable to the Company in accordance with guidelines established for this purpose), bank draft or money order payable to the order of the Company or (2) if so permitted by the Committee at or after the grant of the Option or by the instrument evidencing the Option, (i) through the delivery of shares of Stock which have been held for at least six months (unless the Committee approves a shorter period) and which have a fair market value equal to the exercise price, (ii) by delivery of an unconditional and irrevocable undertaking by a broker to deliver promptly to the Company sufficient funds to pay the exercise price, or (iii) by any combination of the foregoing permissible forms of payment.

(f) Discretionary Payments. If (i) the market price of shares of Stock subject to an Option (other than an Option which is in tandem with a Stock Appreciation Right as described in Section 6.2) exceeds the exercise price of the Option at the time of its exercise, and (ii) the person exercising the Option so requests the Committee in writing, the Committee may in its sole discretion cancel the Option and cause the Company to pay in cash or in shares of Common Stock (at a price per share equal to the fair market value per share) to the person exercising the Option an amount equal to the difference between the fair market value of the Stock which would have been purchased pursuant to the exercise (determined on the date the Option is canceled) and the aggregate exercise price which would have been paid.

## 6.2. STOCK APPRECIATION RIGHTS.

(a) Nature of Stock Appreciation Rights. A Stock Appreciation Right (or "SAR") is an Award entitling the holder on exercise to receive an amount in cash or Stock or a combination thereof (such form to be determined by the Committee) determined in whole or in part by reference to appreciation, from and after the date of grant, in the fair market value of a share of Stock. SARs may be based solely on appreciation in the fair market value of Stock or on a comparison of such appreciation with some other measure of market growth such as (but not limited) to appreciation in a recognized market index. The date as of which such appreciation or other measure is determined shall be the exercise date unless another date is specified by the Committee.

(b) Grant of Stock Appreciation Rights. Stock Appreciation Rights may be granted in tandem with, or independently of, Options granted under the Plan.

(1) Rules Applicable to Tandem Awards. When Stock Appreciation Rights are granted in tandem with Options, (a) the Stock Appreciation Right will be exercisable only at such time or times, and to the extent, that the related Option is exercisable and will be exercisable in accordance with the procedure required for exercise of the related Option; (b) the Stock Appreciation Right will terminate and no longer be exercisable upon the termination or exercise of the related Option, except that a Stock Appreciation Right granted with respect to less than the full number of shares covered by an Option will not be reduced until the number of shares as to which the related Option has been exercised or has terminated exceeds the number of shares not covered by the Stock Appreciation Right; (c) the Option will terminate and no longer be exercisable upon the exercise of the related Stock Appreciation Right; and (d) the Stock Appreciation Right will be transferable only with the related Option.

(2) Exercise of Independent Stock Appreciation Rights. A Stock Appreciation Right not granted in tandem with an Option will become exercisable at such time or times, and on such conditions, as the Committee may specify. The Committee may at any time accelerate the time at which all or any part of the Right may be exercised.

Any exercise of an independent Stock Appreciation Right must be in writing, signed by the proper person and delivered or mailed to the Company, accompanied by any other documents required by the Committee.

6.3. RESTRICTED AND UNRESTRICTED STOCK.

(a) Grant of Restricted Stock. Subject to the terms and provisions of the Plan, the Committee may grant shares of Stock in such amounts and upon such terms and conditions as the Committee shall determine subject to the restrictions described below ("Restricted Stock").

(b) Restricted Stock Agreement. The Committee may require, as a condition to an Award, that a recipient of a Restricted Stock Award enter into a Restricted Stock Award Agreement, setting forth the terms and conditions of the Award. In lieu of a Restricted Stock Award Agreement, the Committee may provide the terms and conditions of an Award in a notice to the Participant of the Award, on the stock certificate representing the Restricted Stock, in the resolution approving the Award, or in such other manner as it deems appropriate.

(c) Transferability and Other Restrictions. Except as otherwise provided in this Section 6.3, the shares of Restricted Stock granted herein may not be sold, transferred, pledged, assigned, or otherwise alienated or hypothecated until the end of the applicable period or periods established by the Committee and the satisfaction of any other conditions or restrictions established by the Committee (such period during which a share of Restricted Stock is subject to such restrictions and conditions is referred to as the "Restricted Period"). Except as the Committee may otherwise determine under Section 7.1 or Section 7.2, if a Participant dies or suffers a Status Change (as defined at Section 7.2(a)) for any reason during the Restricted Period, the Company may purchase the shares of Restricted Stock subject to such restrictions and conditions for the amount of cash paid by the Participant for such shares; provided, that if no cash was paid by the Participant such shares of Restricted Stock shall be automatically forfeited to the Company.

During the Restricted Period with respect to any shares of Restricted Stock, the Company shall have the right to retain in the Company's possession the certificate or certificates representing such shares.

(d) Removal of Restrictions. Except as otherwise provided in this Section 6.3, a share of Restricted Stock covered by a Restricted Stock grant shall become freely transferable by the Participant upon completion of the Restricted Period, including the passage of any applicable period of time and satisfaction of any conditions to vesting. The Committee, in its sole discretion, shall have the right at any time immediately to waive all or any part of the restrictions and conditions with regard to all or any part of the shares held by any Participant.

(e) Voting Rights. Dividends and Other Distributions. During the Restricted Period, Participants holding shares of Restricted Stock granted hereunder may exercise full voting rights and shall receive all regular cash dividends paid with respect to such shares. Except as the Committee shall otherwise determine, any other cash dividends and other distributions paid to Participants with respect to shares of Restricted Stock, including any dividends and distributions paid in shares, shall be subject to the same restrictions and conditions as the shares of Restricted Stock with respect to which they were paid.

(f) Other Awards Settled with Restricted Stock. The Committee may, at the time any Award described in this Section 6 is granted, provide that any or all the Stock delivered pursuant to the Award will be Restricted Stock.

(g) Unrestricted Stock. Subject to the terms and provisions of the Plan, the Committee may grant shares of Stock free of restrictions under the Plan in such amounts and upon such terms and conditions as the Committee shall determine.

(h) Notice of Section 83(b) Election. Any Participant making an election under Section 83(b) of the Code with respect to Restricted Stock must provide a copy thereof to the Company within 10 days of filing such election with the Internal Revenue Service.

#### 6.4. DEFERRED STOCK.

A Deferred Stock Award entitles the recipient to receive shares of Stock to be delivered in the future. Delivery of the Stock will take place at such time or times, and on such conditions, as the Committee may specify. The Committee may at any time accelerate the time at which delivery of all or any part of the Stock will take place. At the time any Award described in this Section 6.4 is granted, the Committee may provide that, at the time Stock would otherwise be delivered pursuant to the Award, the Participant will instead receive an instrument evidencing the Participant's right to future delivery of Deferred Stock.

#### 6.5. PERFORMANCE AWARDS; PERFORMANCE GOALS.

(a) Nature of Performance Awards. A Performance Award entitles the recipient to receive, without payment, an amount in cash or Stock or a combination thereof (such form to be determined by the Committee) following the attainment of Performance Goals (as hereinafter defined). Performance Goals may be related to personal performance, corporate performance, departmental performance or any other category of performance established by the Committee. The Committee will determine the Performance Goals, the period or periods during which performance is to be measured and all other terms and conditions applicable to the Award.

(b) Other Awards Subject to Performance Condition. The Committee may, at the time any Award described in this Section 6.5 is granted, impose the condition (in addition to any conditions specified or authorized in this Section 6 or any other provision of the Plan) that Performance Goals be met prior to the Participant's realization of any payment or benefit under the Award. Any such Award made subject to the achievement of Performance Goals (other than an Option or SAR) shall be treated as a Performance Award for purposes of Section 6.5(c) below.

(c) Limitations and Special Rules. In the case of any Performance Award intended to qualify for the performance-based remuneration exception described in Section 162(m)(4)(C) of the Code and the regulations thereunder (an "Exempt Award"), the Committee shall in writing preestablish specific Performance Goals. A Performance Goal must be established prior to passage of 25% of the period of time over which attainment of such goal is to be measured. "Performance Goal" means criteria based upon any one or more of the following (on a

consolidated, divisional, subsidiary, line of business or geographical basis or in combinations thereof): (i) sales; revenues; assets; expenses; earnings before or after deduction for all or any portion of interest, taxes, depreciation or amortization, whether or not on a continuing operations or an aggregate or per share basis; return on equity, investment, capital or assets; inventory level or turns; one or more operating ratios; borrowing levels, leverage ratios or credit rating; market share; capital expenditures; cash flow; stock price; stockholder return; or any combination of the foregoing; or (ii) acquisitions and divestitures (in whole or in part); joint ventures and strategic alliances; spin-offs, split-ups and the like; reorganizations; recapitalizations, restructurings, financings (issuance of debt or equity) and refinancings; transactions that would constitute a Change of Control; or any combination of the foregoing. A Performance Goal and targets with respect thereto determined by the Committee need not be based upon an increase, a positive or improved result or avoidance of loss. The maximum Exempt Award payable to any Participant in respect of any such Performance Goal for any year shall not exceed \$2,500,000. Payment of Exempt Awards based upon a Performance Goal for the year ending December 31, 2008 and thereafter is conditioned upon reapproval by Employer's shareholders no later than Employer's first meeting of shareholders in the year ending December 31, 2007.

7. EVENTS AFFECTING OUTSTANDING AWARDS

7.1. DEATH.

If a Participant dies, the following will apply:

(a) All Options and Stock Appreciation Rights held by the Participant immediately prior to death, to the extent then exercisable, may be exercised by the Participant's executor or administrator or the person or persons to whom the Option or Right is transferred by will or the applicable laws of descent and distribution, at any time within the one year period ending with the first anniversary of the Participant's death (or such shorter or longer period as the Committee may determine), and shall thereupon terminate. In no event, however, shall an Option or Stock Appreciation Right remain exercisable beyond the latest date on which it could have been exercised without regard to this Section 7. Except as otherwise determined by the Committee, all Options and Stock Appreciation Rights held by a Participant immediately prior to death that are not then exercisable shall terminate at death.

(b) Except as otherwise determined by the Committee, all Restricted Stock held by the Participant must be transferred to the Company (and, in the event the certificates representing such Restricted Stock are held by the Company, such Restricted Stock will be so transferred without any further action by the Participant) in accordance with Section 6.3(c).

(c) Any payment or benefit under a Deferred Stock Award or Performance Award to which the Participant was not irrevocably entitled prior to death will be forfeited and the Award canceled as of the time of death, except as otherwise determined the Committee.

7.2. TERMINATION OF SERVICE (OTHER THAN BY DEATH).

If a Participant who is an Employee ceases to be an Employee for any reason other than death or retirement with consent of the Company after attainment of age 65, or if there is a termination (other than by reason of death) of the consulting, service or similar relationship in respect of which a non-Employee Participant was granted an Award hereunder (such termination of the employment or other relationship being hereinafter referred to as a "Status Change"), the following will apply:

(a) Except as otherwise determined by the Committee, all Options and Stock Appreciation Rights held by the Participant that were not exercisable immediately prior to the Status Change shall terminate at the time of the Status Change. Any Options or Rights that were exercisable immediately prior to the Status Change will continue to be exercisable for a period of three months (or such longer period as the Committee may determine), and shall thereupon terminate, unless the Award provides by its terms for immediate termination in the event of a Status Change (unless otherwise determined by the Committee) or unless the Status Change results from a discharge for cause which in the opinion of the Committee casts such discredit on the Participant as to justify immediate termination of the Award. In no event, however, shall an Option or Stock Appreciation Right remain exercisable beyond the latest date on which it could have been exercised without regard to this Section 7. For purposes of this paragraph, in the case of a Participant who is an Employee, a Status Change shall not be deemed to have resulted by reason of (i) a sick leave or other bona fide leave of absence approved for purposes of the Plan by the Committee, so long as the Employee's right to reemployment is guaranteed either by statute or by contract, or (ii) a transfer of employment between the Company and a subsidiary or between subsidiaries, or to the employment of a corporation (or a parent or subsidiary corporation of such corporation) issuing or assuming an option in a transaction to which Section 424(a) of the Code applies.

(b) Except as otherwise determined by the Committee, all Restricted Stock held by the Participant at the time of the Status Change must be transferred to the Company (and, in the event the certificates representing such Restricted Stock are held by the Company, such Restricted Stock will be so transferred without any further action by the Participant) in accordance with Section 6.3(c) above.

(c) Any payment or benefit under a Deferred Stock Award or Performance Award to which the Participant was not irrevocably entitled prior to the Status Change will be forfeited and the Award cancelled as of the date of such Status Change unless otherwise determined by the Committee.

7.3. CERTAIN CORPORATE TRANSACTIONS.

Except as otherwise provided by the Committee at the time of grant, in the event of a consolidation or merger in which the Company is not the surviving corporation or which results in the acquisition of substantially all the Company's outstanding Stock by a single person or entity or by a group of persons and/or entities acting in concert, or in the event of



the sale or transfer of substantially all the Company's assets or a dissolution or liquidation of the Company (a "covered transaction"), the following rules shall apply:

(a) Subject to paragraph (b) below, all outstanding Awards requiring exercise will cease to be exercisable, and all other Awards to the extent not fully vested (including Awards subject to conditions not yet satisfied or determined) will be forfeited, as of the effective time of the covered transaction, provided that the Committee may in its sole discretion (but subject to Section 7.4), on or prior to the effective date of the covered transaction, (1) make any outstanding Option and Stock Appreciation Right exercisable in full, (2) remove the restrictions from any Restricted Stock, (3) cause the Company to make any payment and provide any benefit under any Deferred Stock Award or Performance Award and (4) remove any performance or other conditions or restrictions on any Award; or

(b) With respect to an outstanding Award held by a participant who, following the covered transaction, will be employed by or otherwise providing services to an entity which is a surviving or acquiring entity in the covered transaction or an affiliate of such an entity, the Committee may at or prior to the effective time of the covered transaction, in its sole discretion and in lieu of the action described in paragraph (a) above, arrange to have such surviving or acquiring entity or affiliate assume any Award held by such participant outstanding hereunder or grant a replacement award which, in the judgment of the Committee, is substantially equivalent to any Award being replaced.

#### 7.4. CHANGE OF CONTROL PROVISIONS.

(a) Impact of Event. Notwithstanding any other provision of the Plan to the contrary, in the event of a Change of Control, and unless otherwise provided for in any certificate or agreement evidencing an Award:

(1) Acceleration of Options and SARs. Any Options and SARs outstanding as of the date such Change of Control is determined to have occurred and which are not then exercisable shall become exercisable to the full extent of the original grant, and all shares of Restricted Stock which are not otherwise vested shall vest. Holders of Performance Awards granted hereunder as to which the relevant performance period has not ended as of the date such Change of Control is determined to have occurred shall be entitled at the time of such Change of Control to receive a cash payment per Performance Award equal to the full value of the cash component of such Award (if any) plus the fair market value of Stock included in such Award.

(2) Restriction on Application of Plan Provisions Applicable in the Event of Termination of Employment. After a Change of Control, Options and SARs shall not be terminated as a result of a termination of employment other than by reason of death, disability (as determined by the Company) or retirement for seven months following such termination of employment or until expiration of the original terms of the Option or SAR, whichever period is shorter.

(3) Restriction on Amendment. In connection with or following a Change of Control, neither the Committee nor the Board may impose additional conditions upon exercise or otherwise amend or restrict an Option, SAR, share of Restricted Stock or Performance Award, or amend the terms of the Plan in any manner adverse to the holder thereof, without the written consent of such holder.

Notwithstanding the foregoing, if any right granted pursuant to this Section 7.4 would make a Change of Control transaction ineligible for pooling of interests accounting under applicable accounting principles that but for this Section 7.4 would otherwise be eligible for such accounting treatment, the Committee shall have the authority to substitute stock for the cash which would otherwise be payable pursuant to this Section 7.4 having a fair market value equal to such cash.

(b) Definition of Change of Control. A "Change of Control" shall be deemed to have occurred if (i) any corporation, person or other entity (other than the Company, a majority-owned subsidiary of the Company, any employee benefit plan maintained by the Company or any of its subsidiaries or members of the Board on the date the Plan is approved by the stockholders of the Company), including a "group" as defined in Section 13(d)(3) of the 1934 Act becomes the beneficial owner of Stock representing more than twenty-five percent of the voting power of the Company (other than by consolidation or merger) or (ii) within any 24 consecutive month period, persons who were members of the Board immediately prior to such 24-month period, together with any persons who were first elected as directors (other than as a result of any settlement of a proxy or consent solicitation contest or any action taken to avoid such a contest) during such 24-month period by or upon the recommendation of persons who were members of the Board immediately prior to such 24-month period and who constituted a majority of the Board at the time of such election, cease to constitute a majority of the Board.

## 8. GENERAL PROVISIONS

### 8.1. DOCUMENTATION OF AWARDS.

Awards will be evidenced by such written instruments, if any, as may be prescribed by the Committee from time to time. Such instruments may be in the form of agreements to be executed by both the Participant and the Company, or certificates, letters or similar instruments, which need not be executed by the Participant but acceptance of which will evidence agreement to the terms thereof.

### 8.2. RIGHTS AS A STOCKHOLDER, DIVIDEND EQUIVALENTS.

Except as specifically provided by the Plan, the receipt of an Award will not give a Participant rights as a stockholder; the Participant will obtain such rights, subject to any limitations imposed by the Plan or the instrument evidencing the Award, only upon the issuance of Stock. However, the Committee may, on such conditions as it deems appropriate, provide that a Participant will receive a benefit in lieu of cash dividends that would have been payable on any or all Stock subject to the Participant's Award had such Stock been

outstanding. Without limitation, the Committee may provide for payment to the Participant of amounts representing such dividends, either currently or in the future, or for the investment of such amounts on behalf of the Participant.

### 8.3. CONDITIONS ON DELIVERY OF STOCK.

The Company will not be obligated to deliver any shares of Stock pursuant to the Plan or to remove restriction from shares previously delivered under the Plan (a) until all conditions of the Award have been satisfied or removed, (b) until, in the opinion of the Company's counsel, all applicable federal and state laws and regulation have been complied with, (c) if the outstanding Stock is at the time listed on any stock exchange or The Nasdaq National Market, until the shares to be delivered have been listed or authorized to be listed on such exchange or market upon official notice of notice of issuance, and (d) until all other legal matters in connection with the issuance and delivery of such shares have been approved by the Company's counsel. If the sale of Stock has not been registered under the Securities Act of 1933, as amended, the Company may require, as a condition to exercise of the Award, such representations or agreements as counsel for the Company may consider appropriate to avoid violation of such Act and may require that the certificates evidencing such Stock bear an appropriate legend restricting transfer.

If an Award is exercised by the Participant's legal representative, the Company will be under no obligation to deliver Stock pursuant to such exercise until the Company is satisfied as to the authority of such representative.

### 8.4. TAX WITHHOLDING.

The Company will withhold from any cash payment made pursuant to an Award an amount sufficient to satisfy all federal, state and local withholding tax requirements (the "withholding requirements").

In the case of an Award pursuant to which Stock may be delivered, the Committee will have the right to require that the Participant or other appropriate person remit to the Company an amount sufficient to satisfy the withholding requirements, or make other arrangements satisfactory to the Committee with regard to such requirements, prior to the delivery of any Stock or removal of restrictions thereon. If and to the extent that such withholding is required, the Committee may permit the Participant or such other person to elect at such time and in such manner as the Committee provides to have the Company hold back from the shares to be delivered, or to deliver to the Company, Stock having a value calculated to satisfy the withholding requirement. The Committee may make such share withholding mandatory with respect to any Award at the time such Award is made to a Participant.

If at the time an ISO is exercised the Committee determines that the Company could be liable for withholding requirements with respect to the exercise or with respect to a disposition of the Stock received upon exercise, the Committee may require as a condition of exercise that the person exercising the ISO agree (a) to provide for withholding under the preceding

paragraph of this Section 8.4, if the Committee determines that a withholding responsibility may arise in connection with tax exercise, (b) to inform the Company promptly of any disposition (within the meaning of section 424(c) of the Code) of Stock received upon exercise, and (c) to give such security as the Committee deems adequate to meet the potential liability of the Company for the withholding requirements and to augment such security from time to time in any amount reasonably deemed necessary by the Committee to preserve the adequacy of such security.

#### 8.5. TRANSFERABILITY OF AWARDS.

Unless otherwise permitted by the Committee, no Award (other than an Award in the form of an outright transfer of cash or Unrestricted Stock) may be transferred other than by will or by the laws of descent and distribution.

#### 8.6. ADJUSTMENTS IN THE EVENT OF CERTAIN TRANSACTIONS.

(a) In the event of a stock dividend, stock split or combination of shares, recapitalization or other change in the Company's capitalization, or other distribution to holders of Stock other than normal cash dividends, after the effective date of the Plan, the Committee will make any appropriate adjustments to the maximum number of shares that may be delivered under the Plan under the first paragraph of Section 4 above and to the limits described in the second paragraph of Section 4 and in Section 6.5(c).

(b) In any event referred to in paragraph (a), the Committee will also make any appropriate adjustments to the number and kind of shares of Stock or securities subject to Awards then outstanding or subsequently granted, any exercise prices relating to Awards and any other provision of Awards affected by such change. The Committee may also make such adjustments to take into account material changes in law or in accounting practices or principles, mergers, consolidations, acquisitions, dispositions or similar corporate transactions, or any other event, if it is determined by the Committee that adjustments are appropriate to avoid distortion in the operation of the Plan; provided, that adjustments pursuant to this sentence shall not be made to the extent it would cause any Award intended to be exempt under Section 162(m)(4)(c) of the Code to fail to be so exempt.

(c) In the case of ISOs, the adjustments described in (a) and (b) will be made only to the extent consistent with continued qualification of the Option under Section 422 of the Code (in the case of an ISO) or Section 162(m) of the Code.

#### 8.7. EMPLOYMENT RIGHTS, ETC.

Neither the adoption of the Plan nor the grant of Awards will confer upon any person any right to continued retention by the Company or any subsidiary as an Employee or otherwise, or affect in any way the right of the Company or subsidiary to terminate an employment, service or similar relationship at any time. Except as specifically provided by the Committee in any particular case, the loss of existing or potential profit in Awards granted

<PAGE> 13

under the Plan will not constitute an element of damages in the event of termination of an employment, service or similar relationship even if the termination is in violation of an obligation of the Company to the Participant.

#### 8.8. DEFERRAL OF PAYMENTS.

The Committee may agree at any time, upon request of the Participant, to defer the date on which any payments under an Award will be made.

#### 8.9. PAST SERVICES AS CONSIDERATION.

Where a Participant purchases Stock under an Award for a price equal to the par value of the Stock the Committee may determine that such price has been satisfied by past services rendered by the Participant.

#### 9. EFFECT, AMENDMENT AND TERMINATION

Neither adoption of the Plan nor the grant of Awards to a Participant will affect the Company's right to grant to such Participant awards that are not subject to the Plan, to issue to such Participant Stock as a bonus or otherwise, or to adopt other plans or arrangements under which Stock may be issued to Employees.

The Committee may at any time or times amend the Plan or any outstanding Award for any purpose which may at the time be permitted by law, or may at any time terminate the Plan as to any further grants of Awards, provided that (except to the extent expressly required or permitted by the Plan) no such amendment will, without the approval of the stockholders of the Company, effectuate a change for which stockholder approval is required in order for the Plan to continue to qualify for the award of ISOs under Section 422 of the Code or for the award of performance based compensation under Section 162(m) of the Code.

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Lynch Corporation Subsidiaries

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Lynch International Holding Corporation	100.0%
Lynch-AMAV LLC	75.0%
M-tron Industries, Inc.	100.0%
M-tron Industries, Ltd.	100.0%
Spinnaker Industries, Inc.	41.8% (O) / 49.5% (V)
Entoleter, Inc.	41.8% (O) / 49.5% (V)
Spinnaker Coating, Inc.	41.8% (O) / 49.5% (V)
Spinnaker Coating-Maine, Inc.	41.8% (O) / 49.5% (V)
Spinnaker Electrical Tape Company	41.8% (O) / 49.5% (V)

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Notes: (O) = Percentage of equity ownership; (V) = Percentage voting control.

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CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in the Registration Statement (Form S-8 No. 33-46953) pertaining to the Lynch Corporation 401(k) Savings Plan of our report dated March 29, 2002, with respect to the consolidated financial statements and schedules of Lynch Corporation included in this Annual Report (Form 10-K) for the year ended December 31, 2001.

/s/ ERNST & YOUNG LLP

-----  
ERNST & YOUNG LLP

Stamford, Connecticut  
March 29, 2002  
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POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, Director and Vice Chairman of the Board of Directors of LYNCH CORPORATION, an Indiana corporation, hereby appoints RALPH R. PAPITTO, RAYMOND H. KELLER and RICHARD E. McGRILL, true and lawful attorneys-in-fact and agents, and each of them (with full power to act without the other) his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign, execute, deliver and file with the Securities and Exchange Commission the Annual Report on Form 10-K of Lynch Corporation for the fiscal year ended December 31, 2001, including any and all amendments thereto, granting unto said attorneys-in-fact and agents, and each of them, full power to do and perform every act and thing requisite, necessary or desirable to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof, and hereby revoking all prior appointments by him, if any, of attorneys-in-fact and agents to sign and file the above-described document, including any and all amendments thereto.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ MARIO J. GABELLI  
 -----  
 MARIO J. GABELLI

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, Director, Chairman of the Board of Directors and Chief Executive Officer of LYNCH CORPORATION, an Indiana corporation, hereby appoints RAYMOND H. KELLER and RICHARD E. McGRAIL, true and lawful attorneys-in-fact and agents, and each of them (with full power to act without the other) his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign, execute, deliver and file with the Securities and Exchange Commission the Annual Report on Form 10-K of Lynch Corporation for the fiscal year ended December 31, 2001, including any and all amendments thereto, granting unto said attorneys-in-fact and agents, and each of them, full power to do and perform every act and thing requisite, necessary or desirable to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof, and hereby revoking all prior appointments by him, if any, of attorneys-in-fact and agents to sign and file the above-described document, including any and all amendments thereto.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ RALPH R. PAPITTO  
 -----  
 RALPH R. PAPITTO

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, Director of LYNCH CORPORATION, an Indiana corporation, hereby appoints RALPH R. PAPITTO, RAYMOND H. KELLER and RICHARD E. McGRAIL, true and lawful attorneys-in-fact and agents, and each of them (with full power to act without the other) his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign, execute, deliver and file with the Securities and Exchange Commission the Annual Report on Form 10-K of Lynch Corporation for the fiscal year ended December 31, 2001, including any and all amendments thereto, granting unto said attorneys-in-fact and agents, and each of them, full power to do and perform every act and thing requisite, necessary or desirable to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof, and hereby revoking all prior appointments by him, if any, of attorneys-in-fact and agents to sign and file the above-described document, including any and all amendments thereto.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ E. VAL CERUTTI  
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 E. VAL CERUTTI

POWER OF ATTORNEY

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IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ AVRUM GRAY  
 -----  
 AVRUM GRAY

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, Director, President and Chief Operating Officer of LYNCH CORPORATION, an Indiana corporation, hereby appoints RALPH R. PAPITTO and RAYMOND H. KELLER, true and lawful attorneys-in-fact and agents, and each of them (with full power to act without the other) his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign, execute, deliver and file with the Securities and Exchange Commission the Annual Report on Form 10-K of Lynch Corporation for the fiscal year ended December 31, 2001, including any and all amendments thereto, granting unto said attorneys-in-fact and agents, and each of them, full power to do and perform every act and thing requisite, necessary or desirable to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof, and hereby revoking all prior appointments by him, if any, of attorneys-in-fact and agents to sign and file the above-described document, including any and all amendments thereto.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ RICHARD E. McGRAIL  
 -----  
 RICHARD E. MCGRAIL

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, Director, Vice President, Chief Financial Officer and Secretary of LYNCH CORPORATION, an Indiana corporation, hereby appoints RALPH R. PAPITTO and RICHARD E. McGRAIL, true and lawful attorneys-in-fact and agents, and each of them (with full power to act without the other) his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign, execute, deliver and file with the Securities and Exchange Commission the Annual Report on Form 10-K of Lynch Corporation for the fiscal year ended December 31, 2001, including any and all amendments thereto, granting unto said attorneys-in-fact and agents, and each of them, full power to do and perform every act and thing requisite, necessary or desirable to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof, and hereby revoking all prior appointments by him, if any, of attorneys-in-fact and agents to sign and file the above-described document, including any and all amendments thereto.

IN WITNESS WHEREOF, the undersigned has hereunto set his hand and seal on the date set forth below.

DATE: March 15, 2002

/s/ RAYMOND H. KELLER  
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 RAYMOND H. KELLER

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April 1, 2002

ELECTRONICALLY FILED

Securities and Exchange Commission  
450 Fifth Street, N.W.  
Judiciary Plaza  
Washington, DC 20001

RE: LYNCH CORPORATION FORM 10-K, DECEMBER 31, 2001

Dear Sir/Madam:

Attached for filing with the Securities and Exchange Commission pursuant to the Securities Act of 1934, as amended, is Lynch Corporation's Form 10-K for the fiscal year ended December 31, 2001.

Please acknowledge receipt of this filing by notifying my e-mail address at Ray.Keller@lynch-mail.com, and notifying jlbomster@apslaw.com.

Very truly yours,

/s/ RAYMOND H. KELLER

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RAYMOND H. KELLER

Enclosures  
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**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**Form 10-K**

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended **December 31, 2001**

Commission file number **1-106**

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

**LYNCH CORPORATION**

*(Exact name of Registrant as specified in its charter)*

**Indiana**

*(State or other jurisdiction of  
Incorporation or organization)*

**38-1799862**

*(I.R.S. Employer  
Identification No.)*

**50 Kennedy Plaza, Suite 1250,  
Providence, RI**

*(Address of principal executive offices)*

**02903**

*(Zip Code)*

**Registrant's telephone number, including area code:  
(401) 453-2007**

**Securities registered pursuant to Section 12(b) of the Act:**

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, No Par Value	American Stock Exchange

**Securities registered pursuant to section 12(g) of the Act: None**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by mark if disclosure of delinquent filers pursuant to Item 405 of Regulations S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K.

The aggregate market value of voting stock held by non-affiliates of the Registrant (based upon the closing price of the Registrant's Common Stock on the American Stock Exchange on March 15, 2002 of \$17.00 per share) was \$17,719,729. (In determining this figure, the Registrant has assumed that all of the Registrant's directors and officers are affiliates. This assumption shall not be deemed conclusive for any other purpose.)

The number of outstanding shares of the Registrant's Common Stock was 1,497,883 as of March 15, 2002.

**DOCUMENTS INCORPORATED BY REFERENCE:**

Part III: Certain portions of Registrant's Proxy Statement for the 2002 Annual Meeting of Shareholders.

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## FORWARD LOOKING INFORMATION

This document contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this discussion and throughout this document, words, such as “intends,” “plans,” “estimates,” “believes,” “anticipates” and “expects” or similar expressions are intended to identify forward-looking statements. These statements are based on the Registrant’s current plans and expectations and involve risks and uncertainties, over which the Registrant has no control, that could cause actual future activities and results of operations to be materially different from those set forth in the forward-looking statements. Important factors that could cause actual future activities and operating results to differ include fluctuating demand for capital goods such as large glass presses, delay in the recovery of demand for components used by telecommunications infrastructure manufacturers, and exposure to foreign economies. Important information regarding risks and uncertainties is also set forth elsewhere in this document, including in Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations”. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Registrant undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. All subsequent written or oral forward-looking statements attributable to the Registrant or persons acting on its behalf are expressly qualified in their entirety by these cautionary statements. Readers are also urged to carefully review and consider the various disclosures made by the Registrant, in this document, as well as the Registrant’s periodic reports on Forms 10-K, 10-Q and 8-K, filed with the Securities and Exchange Commission (“SEC”).

## PART I

### Item 1. *Business*

The Registrant, Lynch Corporation (hereinafter referred to as “Registrant,” “Company” or “Lynch”), incorporated in 1928 under the laws of the State of Indiana, is a diversified holding company with subsidiaries engaged in manufacturing. Lynch’s executive offices are located at 50 Kennedy Plaza, Suite 1250, Providence, RI 02903. Its telephone number is (401) 453-2007.

Lynch has two wholly-owned subsidiaries, M-tron Industries, Inc., a Delaware corporation (“M-tron”), and Lynch Systems, Inc., a South Dakota corporation (“LS” or “Lynch Systems”). Registrant also owns 41.8% of the equity (and 49.5% of the voting power) of Spinnaker Industries, Inc., a Delaware corporation (“Spinnaker”).

Registrant’s business development strategy is to expand its existing operations through internal growth and acquisitions. It may also, from time to time, consider the acquisition of other assets or businesses that are not related to its present businesses. As used herein, the Registrant includes subsidiary corporations.

On September 1, 1999, Registrant spun off to its shareholders the stock of Lynch Interactive Corporation, which holds the multimedia and service operations previously owned by Registrant and which accounted for approximately 40% of the Registrant’s 1998 revenues and 47.6% of Registrant’s total assets at December 31, 1998.

#### A. **Lynch Systems, Inc.**

##### *Overview*

Lynch Systems, Inc. (“LS” or “Lynch Systems”), a 100% owned subsidiary of Registrant, designs, develops, manufactures and markets a broad range of manufacturing equipment for the electronic display and consumer glass industries. LS also produces replacement parts for various types of packaging and glass container-making machines, which LS does not manufacture.

### ***Selected Financial Information***

For financial reporting purposes, Lynch Systems comprises the Registrant's "glass manufacturing equipment" segment. For information about this segment's net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included herein.

### ***Lynch Systems Objectives***

LS intends to continue to build on its name recognition and reputation as one of the world's leading manufacturers of glass forming machinery. LS is the only independent supplier in the CRT (cathode ray tube) glass forming field and it is LS's intention to use this strength to form closer partnerships with its customers in their pursuit of innovative glass making machinery.

LS's long term intentions are to monitor the market direction and to be at the forefront of technology in order to respond to market demand for new and innovative types of machinery needed to produce glass. LS intends to continue to research and develop state-of-the-art machinery within its core competence, and also to seek new markets where its experience and proven success can be utilized to develop new products and increase its growth.

LS also intends to continue to expand on its new expertise obtained from Lynch AMAV in the feeder and shear markets (discussed below) and to reduce the cost of its raw materials by continuing to search for cheaper suppliers of materials, especially from foreign markets. In addition, LS intends to continue its own in-house cost cutting programs by eliminating redundant or superfluous operations, improving its factory quality and yield rates and better utilization of its current personnel. By increasing its efficiency and shortening its delivery rate, LS hopes to increase the number of turns giving a positive effect to its financial performance. There is no assurance that LS can attain these objectives.

### ***Products and Manufacturing***

LS manufactures glass-forming presses and electronic controls to provide high-speed automated systems to form different sizes of face panels and CRT display tubes for television screens and computer monitors including presses to build large screen televisions for the HDTV (high definition television) market. LS also manufactures and installs forming equipment that sizes, cuts, and forms tableware such as glass tumblers, plates, cups, saucers and commercial optical glass. Additionally, LS manufactures and installs fire polishing, electronic controls and retrofit systems for CRT display and consumer glass presses.

At year-end 1998, LS, through a subsidiary, entered into a joint venture, Lynch-AMAV LLC, with AMAV GmbH of Germany to develop and manufacture glass-manufacturing equipment for the tableware industry. LS has a 75% interest in the joint venture. The joint venture designs and develops feeders, shears and presses, most of which are manufactured for the joint venture by LS. LS believes that this joint venture has expanded LS's glass tableware equipment business, particularly in Europe.

The production of glassware entails the use of machines, which heat glass and, using great pressure, form an item by pressing it into a desired shape. Because of the high cost of bringing the machine and materials up to temperature, a machine for producing glassware must be capable of running 24 hours a day, 365 days a year.

During 2001, LS, including Lynch-AMAV, built TV (television) and consumer glass press machines for customers, as well as selling feeders, shears and spare parts. LS delivered four large TV glass press machines in 2001. These four large machines had a selling price of approximately \$14 million, all of which was recognized as income in 2001. In 2001 LS sold four additional large TV glass press machines to be delivered in 2002. These additional machines sold for approximately \$14 million, of which \$5.5 million was recognized as income in 2001 using the percentage of completion method and the balance of \$8.5 million will be recognized in 2002.

At December 31, 2001, LS had orders for \$12 million for large TV glass press machines as well as for glass press machines, feeders, shears and spare parts for the tableware market, all of which are scheduled to be

delivered in 2002. LS is also in negotiations to obtain other orders for large TV glass presses; however, there can be no assurance that LS will obtain any other orders.

LS's worldwide customers require capital equipment that produces a wide variety of Tableware products to remain competitive. In support of this market demand, Lynch Systems has invested in R&D programs to manufacture new lines of capital equipment such as Stretch Machines for one-piece Stemware, Firepolishers for high quality Tableware and Spinning Machines for high speed, high quality Dishware.

To further expand LS's Tableware product lines, additional product lines have been acquired through royalty partnerships with leading Industry concerns. In 1999, LS acquired the H-28 Press and Blow machine from Emhart. This high production machine produces both round and geometric design Tumblers and is now marketed by LS as the LH-28 with numerous Electronic Control improvements. In 2000, the Eldred product line of Burnoff Machines, used to fire finish the rims of the H-28 Tumblers, and four-color Decorating Machines were acquired by LS. All Tableware capital equipment requires moulds in the production of any article. In 2002, agreement was reached with Merkad, a producer of high quality moulds, to represent and distribute moulds throughout North and South America.

LS has the capabilities to take a glass product idea from a customer, have our engineering staff design a machine that will mass produce this glass product and then build the final machine for the customer.

#### ***International Sales***

LS's revenues from international sales were \$22.9 million, \$20.3 million and \$4.7 million for 2001, 2000 and 1999, respectively, representing approximately 88%, 88% and 83% of LS's net sales for 2001, 2000 and 1999, respectively. The profitability of international sales is approximately equivalent to that of domestic sales. Because many international orders require partial advance deposits, with the balance often secured by irrevocable letters of credit from banks in the foreign country, the Registrant believes that some of the credit risks commonly associated with doing business in international markets are minimized. The Registrant avoids currency exchange risk by transacting substantially all international sales in United States dollars.

#### ***Backlog***

LS had an order backlog of approximately \$12 million at December 31, 2001, compared with approximately \$13.5 million at December 31, 2000. All of LS's \$12 million backlog as of December 31, 2001 is scheduled to be delivered in 2002. LS includes as backlog only those orders which are subject to written contract or written purchase orders. In 1998, LS received \$2.4 million in connection with the cancellation of a \$16 million dollar order for large TV glass presses and parts, which amount can be used by the customer as a credit for future orders. The \$2.4 million has been reduced to \$1.5 million as of December 31, 2001 as a result of sales to this customer.

#### ***Competition***

LS believes that in the worldwide pressware market it is the largest supplier to glass companies that do not manufacture their own pressware machines. Competitors include various companies in Italy, Japan, Korea, Germany and elsewhere. While several of the largest domestic and international producers of glass pressware frequently build their own glass-forming machines and produce spare parts in-house, nearly all pressware producers have made purchases of machines and/or spare parts from LS.

#### ***Customers***

LS's business is not dependent upon a single customer or a few customers.

#### ***Raw Materials***

Raw materials are generally available to LS in adequate supply from a number of suppliers.

### ***Research and Development***

Research and development expense was \$146,000 in 2001 and zero in each of 2000 and 1999. R&D expense for 2002 is budgeted at \$100,000.

### ***Intellectual Property***

Lynch Systems owns patents and proprietary know-how which are important to its business and the maintenance of its competitive position. Its most important patent is for a rotary glass-molding press with cushioned trunnion mounted hydraulic drive, expiring October, 2012. Lynch System's investment in Lynch-AMAV, discussed above, has given Lynch Systems access to important proprietary know-how and technology which has enabled Lynch Systems to expand its product offerings and customer base.

### ***Employees***

Lynch Systems employs approximately 93 employees at its Bainbridge, Georgia facility and 7 employees at Lynch-AMAV in Germany, none of whom belong to a union.

## **B. M-tron Industries, Inc. ("M-tron")**

### ***Overview***

M-tron, a wholly-owned subsidiary of Lynch, is a designer, manufacturer and marketer of custom designed electronic components that are used primarily to control the frequency or timing of electronic signals in communications equipment. Its devices, which are commonly called frequency control devices, crystals or oscillators, support fixed and mobile wireless, copper wire, coaxial cable, wide area networks, local area networks and fiber optic systems. It sells its products to original equipment manufacturers, contract manufacturers and to distributors.

M-tron's products are quartz crystal based frequency control devices consisting of packaged quartz crystals and oscillators incorporating those crystals. Its products enable communications equipment manufacturers and network equipment manufacturers to meet the increasing demands of their customers because they produce an electrical signal that is:

- accurate — the frequency of the signal does not change significantly over a period of time;
- stable — the frequency of the signal does not vary significantly when our product is subjected to a range of operating temperatures; and
- has low electronic noise — the signal does not add interfering signals that can degrade the performance of the electronics system.

In addition, M-tron sells crystals and oscillators which are used outside the communications industry. These frequency control devices are used in microprocessor and computer applications, industrial controls, medical instrumentation, automotive products and military applications.

M-tron has over 35 years of experience designing, manufacturing and marketing crystal based frequency control products. Its customers rely on the skills of M-tron's engineering and design team to help them solve frequency control problems during all phases of their product's life cycles, including product design, prototyping, manufacturing and subsequent product improvements.

### ***Selected Financial Information***

For financial reporting purposes, M-tron comprises the Registrant's "frequency control devices" segment. For information about this segment's net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included herein.



### *M-tron Objectives*

M-tron's objective is to build on the strength of its core expertise in packaged quartz crystal and oscillator technologies to become the supplier of choice to original equipment manufacturers who supply infrastructure equipment to the communications and networking industries.

M-tron intends to maintain its current investment in technical resources, including design and engineering personnel to enable it to provide a high level of design and engineering support to its customers. It believes that technical participation with its original equipment manufacturers customers in the early stages of their design process will lead to M-tron's frequency control devices being designed into their products more regularly.

M-tron intends to increase the use of its offshore contract manufacturers who have added capacity on its behalf. However, during the current economic slowdown, this additional capacity is not being fully utilized. In addition, M-tron's long term objective is to reduce the time it takes to manufacture its products which will result in further increases in its manufacturing capacity. To that end, it has dedicated additional resources to evaluating its manufacturing processes and to identifying and implementing process improvements.

M-tron believes that it can significantly enhance its business opportunities by acquiring technology, product portfolios and/or customer bases. Some of these may offer immediate sales opportunities while others may meet longer term objectives. It plans to pursue these opportunities by making strategic acquisitions or by acquiring or licensing technology.

M-tron intends to design, manufacture and sell devices that offer higher frequencies or greater precision than its current products. These devices will serve applications within the communications and networking industries for which it does not currently provide products. It intends to achieve this through a combination of focused research and development and strategic acquisitions, if they are appropriate.

There is no assurance that M-tron can achieve these objectives.

### *Products*

M-tron's products are high quality, reliable, technically advanced frequency control devices, including packaged quartz crystals and oscillators incorporating those crystals.

M-tron designs and produces a range of packaged quartz crystals and quartz crystal based oscillators. There are a variety of features in its product family. The Packaged Crystal is a single crystal in a hermetically sealed package and is used by electronic equipment manufacturers, along with their own electronic circuitry, to build oscillators for frequency control in their electronic devices. The Clock Oscillator is the simplest of its oscillators. It is a self-contained package with a crystal and electronic circuitry that is used as a subsystem by electronic equipment manufacturers to provide frequency control for their devices. The Voltage Controlled Crystal Oscillator (VCXO) is a variable frequency oscillator whose frequency can be changed by varying the control voltage to the oscillator. The Temperature Compensated Crystal Oscillator (TCXO) is an oscillator designed for use over a range of temperatures. The Digitally Compensated Crystal Oscillator (DCXO) is a temperature compensated oscillator in which the compensation electronics are digital and offer greater frequency stability than the TCXO over a range of temperatures. This variety of features in M-tron's product family offers the designers at electronic equipment manufacturers a range of options as they create the needed performance in their products.

Currently, M-tron's oscillator products operate at frequencies ranging from 32 kilohertz to over 800 megahertz which constitute most of the oscillator frequencies that are now used in communications equipment. However, many of its products, through amplification or other means, are ultimately incorporated into those products that operate at frequencies in excess of 800 megahertz.

M-tron's products are employed in numerous applications within the communications industry, including computer and telephone network switches, high-speed gigabit Ethernet, modems, wireless transmitters/receivers, multiplexers, data recovery/regeneration devices, fiber channel networks, repeaters, data

transceivers, line interface devices and base station controllers. Its products are incorporated into end products that serve all elements of the communications industry.

The crystals and oscillators M-tron sells for use in non-communications applications are used in industrial applications such as security systems, metering systems, electronic test instruments and industrial control systems. They are used in military and medical instrumentation applications as well as in various computer peripheral equipment such as printers, modems, monitors, video cards and sound cards. These non-communications applications may not require the quality and reliability demanded by manufacturers of communications equipment.

#### ***Research and Development***

At December 31, 2001, M-tron employed 10 engineers and technicians in South Dakota who devoted most of their time to research and development. M-tron intends to maintain the number of engineers and technicians who perform research and development in 2002. Its research and development expense was approximately \$1,348,000 in 2001, \$994,000 in 2000 and \$856,000 in 1999. At its current level of resources, which is reduced from the level of 2001, M-tron expects to reduce its spending on research and development by 25% during 2002.

#### ***Customers***

M-tron markets and sells its frequency control devices primarily to:

- original equipment manufacturers of communications and networking equipment;
- contract manufacturers for original equipment manufacturers; and
- distributors who sell to original equipment manufacturers and contract manufacturers.

In 2001, Celestica (with Primetech) accounted for approximately 14% of M-tron's net sales, compared to less than 10% in 2000. No other customer accounted for more than 10% of its 2001 revenues. Sales to its ten largest customers accounted for approximately 60% of net sales for 2001, 2000 and 1999.

#### ***International Sales***

M-tron's revenues from international sales were \$9.5 million, \$17.6 million and \$11.3 million for 2001, 2000 and 1999, respectively, representing approximately 44%, 48% and 43% of its net sales for 2001, 2000 and 1999, respectively. In 2001, this consisted of approximately 27% from customers in Canada, 11% from customers in Asia, 4% from customers in Western Europe and 2% from customers in Mexico. M-tron is increasing its international sales efforts by adding distributors and manufacturers' representatives in Western Europe and Asia.

#### ***Backlog***

M-tron had backlog orders of approximately \$1.4 million at December 31, 2001 compared with approximately \$12.4 million at December 31, 2000. However, monthly new orders for the first two months of 2002 were 20% higher than the average monthly orders for the last three months of 2001. M-tron includes as backlog those orders which are subject to specific production release orders under written contracts, verbal and written orders from distributors with which it has had long-standing relationships, as well as written purchase orders from sales representatives. Its customers may cancel or defer orders without significant penalty.

#### ***Competition***

Frequency control devices are sold in a highly competitive industry. There are numerous domestic and international manufacturers who are capable of providing custom designed quartz crystals and oscillator modules comparable in quality and performance to its products. Competitors include Vectron International (a division of Dover Corporation), CTS Corporation and Saronix. M-tron does not operate in the same markets as high volume manufacturers of standard products; rather it focuses on manufacturing lower volumes of

custom designed frequency control devices. Many of its competitors and potential competitors have substantially greater financial, engineering, manufacturing and marketing resources than it does. M-tron seeks to manufacture custom designed, high performance crystals and oscillators, which it believes it can sell competitively based upon performance, quality, order response time and a high level of engineering support.

### ***Manufacturing***

M-tron has one manufacturing facility in Yankton, South Dakota, and has long-term relationships with two contract manufacturers in Asia. M-tron maintains a rigorous quality control system and is an ISO 9001 qualified manufacturer.

In 1990, M-tron established a working relationship with a contract manufacturer located in South Korea, and in 1994, it established a working relationship with a contract manufacturer located in the People's Republic of China. While it does not have written long term agreements with them, it believes that it is the largest customer for each of these contract suppliers and, as such, believes that from time to time it received preferential treatment on production scheduling matters.

M-tron attempts to utilize standard parts and components that are available from multiple vendors located in the United States or internationally; however, some components used in its products are available from only a limited number of sources.

### ***Intellectual Property***

M-tron has no patents, trademarks or licenses which are considered to be important to M-tron's business or operations. Rather, M-tron believes that its technological position depends primarily on the technical competence and creative ability of its engineering and technical staff in areas of product design and manufacturing processes as well as proprietary know-how and information.

### ***Employees***

As of December 31, 2001, M-tron employed 136 people. It has also employed independent contractors and temporary employees. None of its employees is represented by a labor union and it considers its employee relations to be good.

## **C. Spinnaker Industries, Inc. ("Spinnaker")**

Lynch (through its subsidiary LS) currently owns 1,829,063 shares of the Class A Common Stock and 1,237,203 shares of the Common Stock of Spinnaker Industries, Inc. ("Spinnaker"). Lynch's combined holdings in Spinnaker represent 41.8% and 49.5% of the equity and voting power of Spinnaker, respectively. Spinnaker conducts its business through two wholly-owned subsidiaries, Spinnaker Coating, Inc. ("Spinnaker Coating") and Entoleter, Inc. ("Entoleter").

### ***Deconsolidation***

Prior to September 30, 2001, Lynch owned 48% and 60%, respectively, of the equity and voting power of Spinnaker. As such, under accounting principles generally accepted in the United States, Lynch consolidated the results of Spinnaker and was required to record all of the losses of Spinnaker, since the non-Lynch interests were not required to absorb their shares of losses (52%) after their investment was fully absorbed by losses. On September 26, 2001, Lynch caused LS to make a charitable disposition of 430,000 shares of Spinnaker's Class A Common Stock. As a result of that transaction: (a) Lynch's equity interest and voting power in Spinnaker were reduced to their current level of 41.8% and 49.5%, respectively, (b) Lynch deconsolidated Spinnaker for financial reporting purposes, effective September 30, 2001, (c) since September 30, 2001, Lynch has accounted for its ownership of Spinnaker using the equity method of accounting and (d) Lynch will not record any additional losses from Spinnaker, as Lynch has no obligation to further fund such losses.

### ***Spinnaker Chapter 11 Reorganization Proceeding***

On November 13, 2001 (the “Filing Date”), Spinnaker and its Spinnaker Coating, Spinnaker Coating-Maine, Inc. and Entoleter subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code (11 U.S.C. §101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the “Court”). The cases are being jointly administered under Case No. 01-38066.

Effective December 28, 2001, Spinnaker’s Common Stock and Class A Common Stock were de-listed from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligation to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the “Letter of Intent”) with WR Capital Partners, LLC (“WR Capital”) whereby SP Acquisition LLC (“SP Acquisition”), an acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker’s (and its subsidiaries’) assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations). Entoleter’s assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement (as amended, the “Asset Purchase Agreement”) with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker’s assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker’s equity holders.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter’s assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 5, 2002. If the sale closes, Spinnaker estimates that pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter’s sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (i) and (ii), liquidate Entoleter’s assets.

Spinnaker’s business and properties are described below (in this Section C of Item 1 and in Item 2) without regard to the impact of Spinnaker’s reorganization proceeding and the sale of its assets pursuant thereto.

#### ***Business***

Spinnaker, through Spinnaker Coating, is a manufacturer and marketer of adhesive-backed material, primarily for the pressure sensitive label stock market.

Spinnaker Coating primarily manufactures custom, low-volume, pressure sensitive products used for specialty applications. Customers convert its label stock into labels used for a broad range of end use applications, including bar-coding, mailing and shipping, packaging for pharmaceutical, food and other consumer products, office identification and business forms, postage stamps, decorative labels and other specialty industrial uses. Spinnaker Coating is the largest supplier of pressure sensitive postage stamp stock for ultimate use by the United States Postal Service. In March 1998, Spinnaker Coating was selected by Paper Corporation of the U.S. (“PCUS”) to be its exclusive source of pressure sensitive postage stamp stock for delivery under a five year supply contract it was awarded by the U.S. Bureau of Engraving and Printing. Spinnaker also supplies, through PCUS, pressure sensitive postage stamp stock to private printers who supply postage stamps directly to the United States Postal Service.

In March 1998, Spinnaker Coating acquired the pressure sensitive manufacturing facilities of S.D. Warren Company (“Warren”) in Westbrook, Maine for an aggregate purchase price of approximately

\$51.8 million plus the assumption of certain liabilities (excluding substantially all trade payables). The purchase price was paid by the issuance of a subordinated convertible note to Warren, in the original principal amount of \$7.0 million, and the remainder with funds available under Spinnaker's asset-backed working capital revolving credit. The facility became unprofitable and was closed in July 2001.

Spinnaker also manufactures and markets industrial process equipment and air pollution control scrubbers through Entoleter.

#### ***Selected Financial Information***

For financial reporting purposes, until September 30, 2001 when Spinnaker was deconsolidated from Registrant, Spinnaker Coating comprised the Registrant's "adhesive-backed label stock" segment and Entoleter comprised the "industrial process equipment" segment. For information about these segments' net sales, profit or loss, and total assets for each of the last three fiscal years, please see Note 15 "Segment Information" to the Registrant's Consolidated Financial Statements included in this report.

#### ***Adhesive-backed Label Stock***

Spinnaker Coating develops, manufactures and markets pressure sensitive adhesive-backed label stock that is converted by printers and industrial users into products that are utilized for marking, identifying, labeling and decorating applications and products. To better concentrate on Spinnaker Coating's strengths and market niche, a decision was made by Spinnaker's management to reorganize and realign the business in the fourth quarter of 2000 and going forward in 2001. The restructuring involved the elimination of non-pressure sensitive product lines, outsourcing of non-core manufacturing processes and termination of approximately 100 employees.

Pressure sensitive products, which are activated by the application of pressure, are manufactured with a three-element construction consisting of face stock, adhesive coating and silicone coated release liner. The adhesive product is sold in roll or sheet form for further conversion into products used primarily for marking, identification and promotional labeling. Spinnaker Coating's pressure sensitive products are sold under the trade names Strip Tac® and Strip Tac Plus®. Roll pressure sensitive products are generally sold to label printers that produce products used primarily for informational labels (shipping labels, price labels, warning labels, etc.), product identification and postage stamps. Sheet pressure sensitive products are sold to commercial sheet printers, who provide information labels and other products (such as laser printer stock).

#### ***Marketing and Customers***

Spinnaker Coating markets its broad range of products to a variety of customers. Its marketing strategy focuses not only on products but also customer service and specific customer applications. Spinnaker has conducted business with its top 10 customers for approximately 20 years on average. During 2001, one customer, Paper Corporation of the United States, accounted for approximately 17.1% of Spinnaker's net sales.

Spinnaker Coating generally markets its products through its own sales representatives to regional and national printers, converters and merchants. A major portion of sales represent product manufactured and shipped to customers directly from Spinnaker Coating's facilities in Troy, Ohio. However, to broaden its market penetration, Spinnaker Coating also contracts with regional processors throughout the United States, with whom Spinnaker Coating stores product until sold. Generally, these processors perform both slitting and distribution services for Spinnaker Coating.

#### ***Manufacturing and Raw Materials***

Spinnaker Coating manufactures its adhesive-backed label stock products at two plants in Troy, Ohio. Spinnaker has made approximately \$8.4 million in capital expenditures at the Ohio facilities over the last five years.

Raw materials are the most significant cost component in Spinnaker Coating's production process. The material component accounts for approximately 65-75% of the total cost of its products, with the most important raw materials being paper (gumming kraft and face stock), adhesive materials, and polypropylene film. These materials are currently readily available and are procured from numerous suppliers. The cost of Spinnaker's principal raw materials have generally remained stable or decreased over recent years. Historically, the increases in raw material costs for Spinnaker's products have not materially impacted Spinnaker's gross margin. The future impact of a change in raw material costs on Spinnaker's profitability is based, in part, on pricing by Spinnaker's competitors. Although, changes in Spinnaker's raw material costs have recently not materially impacted Spinnaker's gross margin, Spinnaker cannot be assured that future raw material cost increases can be passed through to its customers or that such cost increases will not negatively impact Spinnaker's gross margin.

### ***Competition***

The adhesive-backed label stock industry is highly competitive. Spinnaker Coating competes with several national manufacturers, including the Fasson unit of Avery Dennison and the MACtac unit of Bemis Company, Inc., as well as a number of importers and smaller regional manufacturers. As a result of the competitive environment in the markets in which Spinnaker Coating operates, the company faces (and will continue to face) pricing pressure on its products. As a result of such pricing pressure, Spinnaker Coating has experienced, and may continue to experience, reductions in the profit margins on its sales, or has and may be unable to pass future raw material price increases to its customers (which would also reduce profit margins).

### ***Backlog***

Spinnaker Coating's label stock backlog believed to be firm was \$5.0 million at December 31, 2001, as compared to \$8.4 million at December 31, 2000.

### ***Industrial Process Equipment Business***

Through Entoleter, Spinnaker engineers, manufactures and markets a line of industrial process equipment and a line of air pollution control equipment. Entoleter's net sales consist entirely of sales to commercial and industrial customers.

### ***Environmental Regulations***

Spinnaker's operations are subject to environmental laws and regulations governing emissions to the air, discharges to waterways, and generation, handling, storage, transportation, treatment and disposal of waste materials. Spinnaker is also subject to other federal and state laws and regulations regarding health and safety matters. Environmental laws and regulations are constantly evolving and it is impossible to predict the effect that these laws and regulations will have on Spinnaker in the future. While Spinnaker believes it is currently in substantial compliance with all such environmental laws and regulations, there can be no assurance that it will at all times be in complete compliance with all such requirements. Spinnaker has made, and expects to continue to make, capital expenditures to comply with environmental requirements. As is the case with manufacturers in general, if a release of hazardous substances occurs on or from Spinnaker's properties or any associated offsite disposal location, or if contamination from prior activities is discovered at any of Spinnaker's properties, Spinnaker may be held liable and the amount of such liability could be material.

### ***Patents and Trademarks***

Patents are held by Spinnaker with respect to the manufacture of certain of its products, but its management does not consider such patents to be important to Spinnaker's operations. The patents expire over various lengths of time with the last patent expiring in about 10 years. Spinnaker has registered several of its trade names and trademarks for adhesive-backed materials.

### ***International Sales***

Spinnaker's international sales were \$13.3 million, \$20.1 million and \$17.5 million in 2001, 2000 and 1999, respectively, representing approximately 11.4%, 17.4%, and 10.8% of Spinnaker's net sales for 2001, 2000 and 1999, respectively. Of the \$13.3 million in 2001 international sales, approximately 99% were represented by exports of Spinnaker Coating. The substantial majority of these sales were to Canadian customers and, consequently, Spinnaker believes that the risks commonly associated with doing business in international countries are minimal. The gross margin on international sales is substantially equivalent to that of domestic sales. Because international sales are transacted in United States dollars, payments in many cases are secured by irrevocable letters of credit.

### ***Employees***

As of December 31, 2001, Spinnaker employed 263 persons, of whom 231 were Spinnaker Coating employees and 32 were Entoleter employees. Spinnaker Coating's Troy, Ohio plants began negotiating a collective bargaining agreement with the Paper, Allied Industrial, Chemical and Energy Workers International Union, AFL-CIO ("PACE") in February 2001, but have yet to reach an agreement. This agreement will cover approximately 132 hourly employees. Entoleter's approximately 14 hourly production employees are members of the United Electrical, Radio and Machine Workers of America Union. The current collective bargaining agreement expires in 2002. Spinnaker and Entoleter believe that their relations with their employees are good; however, there can be no assurance that they will not experience work stoppages or slowdowns in the future.

### **D. Other Information**

While the Registrant holds licenses and patents of various types, Registrant does not believe they are critical to its overall operations. See respective "Intellectual Property" sections for each of Lynch Systems, M-tron and Spinnaker above.

The Registrant conducts product development activities with respect to each of its major lines of business. Currently, such activities are directed principally toward the improvement of existing products, the development of new products and/or diversification. In the last three years, M-tron has accounted for the vast majority of Registrant's product development costs.

The capital expenditures, earnings and competitive position of Registrant have not been materially affected to date by compliance with current federal, state, and local laws and regulations relating to the protection of the environment; however, Registrant cannot predict the effect of future laws and regulations. The Registrant has not experienced difficulties relative to fuel or energy shortages. See also "Environmental Regulations" under Item 1. Business — C. Spinnaker Industries, Inc. for more information with respect to Spinnaker.

No portion of the business of the Registrant is regarded as seasonal.

There were no customers in 2001 or 2000 that represent 10% or more of consolidated revenues. The Registrant does not believe that it is dependent on any single customer.

Additional information with respect to each of the Registrant's lines of business is included in Note 15 to the Consolidated Financial Statements included as Item 14(a) below.

### **E. Executive Officers of the Registrant**

Pursuant to General Instruction G (3) of Form 10-K, the following list of executive officers of the Registrant is included in Part I of this Annual Report on Form 10-K in lieu of being included in the Proxy Statement for the 2002 Annual Meeting of Shareholders. Such list sets forth the names and ages of all executive officers of Registrant indicating all positions and offices with the Registrant held by each such person and each such person's principal occupations or employment during the past five years.

<u>Name</u>	<u>Offices and Positions Held</u>	<u>Age</u>
Ralph R. Papitto . . . . .	Chairman and Chief Executive Officer (since August 2001) of Lynch; Chief Executive Officer of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2000); Chairman and Chief Executive Officer of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1990-1999); Founder, Chairman and Chief Executive Officer of Nortek, Inc., a NYSE listed manufacturer of construction products (1967-1990); Director of Lynch Interactive Corporation (since 1999); Spinnaker Industries, Inc.; AFC Cable Systems, Inc.; and Global Sports & Gaming.Com; Chairman of the Board of Trustees of Roger Williams University.	75
Mario J. Gabelli . . . . .	Chairman (1986 to August 2001) and Chief Executive Officer (1986 to January 2000; and April 2001 to August 2001) and Vice Chairman (since August 2001) of Lynch; Chairman, Chief Executive Officer and a Director of Lynch Interactive Corporation (since September 1999); Chairman and Chief Executive Officer of Gabelli Group Capital Partners (since 1980), a private Corporation which makes investments for its own account; Chairman and Chief Executive Officer of Gabelli Asset Management Inc. (since 1999), a NYSE listed holding corporation for subsidiaries engaged in various aspects of the securities business; Director/Trustee and/or President of all registered investment companies managed by Gabelli Funds, LLC (since 1986); Governor of the American Stock Exchange; Overseer of Columbia University Graduate School of Business; Trustee of Fairfield University, Roger Williams University, Winston Churchill Foundation and E.L. Wigend Foundation; Director of The National Italian American Foundation and The American-Italian Cancer Foundation, Chairman, Patron's Committee of Immaculate Conception School; and former trustee of Fordham Preparatory School.	59
Richard E. McGrail . . . .	President and Chief Operating Officer (since October 2001) of Lynch; President of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2001); Division President of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1993 to 2001); Prior general and marketing management experience with Digital Equipment Corporation (DEC).	47
Raymond H. Keller . . . .	Chief Financial Officer, Vice President and Secretary (since October 2001) of Lynch; Chief Financial Officer of Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto (since 2000); Director and Chief Financial Officer of AFC Cable Systems, Inc., a NASDAQ listed manufacturer and supplier of electrical distribution products (1989 to 2000); Trustee of Roger Williams University; Prior financial management experience with Microdot, Inc.	64



The executive officers of the Registrant are elected annually by the Board of Directors at its organizational meeting in May and hold office until the organizational meeting in the next year and until their respective successors are chosen and qualified.

**Item 2. *Properties***

Lynch's principal executive offices in Providence, Rhode Island are leased and shared with Avtek Inc., a private holding company co-owned by Mario J. Gabelli and Ralph R. Papitto. Mr. Gabelli is Vice Chairman and a Director of Lynch. Mr. Papitto is Chairman and Chief Executive Officer of Lynch.

During 2000 Spinnaker moved its corporate headquarters from Dallas, Texas to Troy, Ohio, where it has major facilities.

Spinnaker Coating owns two manufacturing facilities, Plant One and Plant Two, in Troy, Ohio. Plant One is a 200,000 square foot complex and Plant Two is a 98,000 square foot facility. The facilities house manufacturing, administrative and shipping operations.

In connection with Spinnaker Coating's acquisition of the Warren facilities in March 1998, the parties entered into a site lease, which provides for Warren's lease of a portion of its Westbrook, Maine facility to Spinnaker. Such lease is for a term of 99 years, provides for nominal rent of \$1.00 per year, with an option to purchase for \$1.00. The facility contains approximately 50,000 square feet. With Spinnaker Coating's closure of its Maine business in July 2001, the facility is currently vacant and efforts are being made to sublease or sell the property. Spinnaker's plants are subject to security interests relating to its indebtedness.

Entoleter owns a manufacturing plant containing 72,000 square feet located on approximately 5 acres of land in Hamden, Connecticut. The land and building are subject to a mortgage and security agreement executed in support of a bank loan. Entoleter also owns approximately 6 unimproved acres located in Hamden, Connecticut adjacent to its property.

LS's operations are housed in two adjacent buildings situated on 3.19 acres of land in Bainbridge, Georgia. In January 1997, LS completed an expansion of its manufacturing capacity at this site, which added approximately 15,000 square feet, bringing total manufacturing space to approximately 73,000 square feet. Finished office area in the two buildings totals approximately 17,000 square feet. All such properties are subject to security deeds relating to loans.

Lynch-Amav located in Germany leases certain real and personal property under a commercial lease agreement that expires in December 2003. The lease agreement is between Lynch-Amav and the minority joint venture member's family and provides for annual lease payments of \$120,000.

M-tron's operations are housed in two separate facilities in Yankton, South Dakota. These facilities contain approximately 51,000 square feet in the aggregate. One facility owned by M-tron contains approximately 35,000 square feet and is situated on approximately 15 acres of land. The other Yankton facility containing approximately 16,000 square feet is leased, which lease expires on September 30, 2003, with options to extend the lease to 2006.

It is Registrant's opinion that the facilities referred to above are in good operating condition and suitable and adequate for present uses.

**Item 3. *Legal Proceedings***

In the normal course of business subsidiaries of the Registrant are defendants in certain product liability, worker claims and other litigation in which the amounts being sought may exceed insurance coverage levels. The resolution of these matters is not expected to have a material adverse effect on the Registrant's

consolidated financial condition or operations. In addition, Registrant and/or one or more of its subsidiaries are parties to the following additional legal proceedings:

**1. In re Spinnaker Coating, Inc., Debtor/PACE Local 1-1069 v. Spinnaker Coating, Inc., and Lynch Corporation, U.S. Bankruptcy Court, District of Maine, Chapter 11, Adv. Pro. No. 02-2007; and PACE Local 1-1069 v. Spinnaker Industries, Inc., Spinnaker Coating, Inc., and Spinnaker Coating-Maine, Inc., Cumberland County Superior Court, CV-2001-00352:**

On or about June 26, 2001, in anticipation of the July 15, 2001 closure of Spinnaker's Westbrook, Maine facility, Plaintiff PACE Local 1-1069 filed a three count complaint in Cumberland County Superior Court, CV-2001-00352 naming the following defendants: Spinnaker Industries, Inc., Spinnaker Coating, Inc., and Spinnaker Coating-Maine, Inc. (collectively, the "Spinnaker Entities") and Lynch. The complaint alleged that under Maine's Severance Pay Act both the Spinnaker Entities and Lynch would be liable to pay approximately \$1,166,000 severance pay under Maine's Severance Pay Act in connection with the plant closure. The Defendants filed a notice of removal, thereby creating United States District Court Civil Action C.V. No. 01-236. The case was remanded to state court. The Spinnaker Entities also filed a separate complaint challenging the constitutionality of the Maine Severance Pay Act, United States District Court Civil Action No. 01-232. Thereafter, when the Spinnaker Defendants filed for relief under Chapter 11 of the Bankruptcy Code, they filed a second notice of removal, creating United States District Court for the District of Maine case number C.V. No. 02-7. Upon entry of an order confirming automatic reference, the C.V. No. 02-7 was referred to the United States Bankruptcy Court, District of Maine, and assigned Adv. Pro. No. 02-2007. This litigation was resolved as follows:

- i) To the extent the United States District Court Civil Action No. 01-236 and 02-7 had not already been closed, the parties agreed to, as necessary, stipulations of dismissal disposing of those actions;
- ii) The Spinnaker Entities stipulated to dismissal with prejudice, without costs, of United States District Court Civil Action No. 01-232;
- iii) In Adv. Pro. No. 02-2007, Count I of the Plaintiff's complaint was dismissed with prejudice and without costs to any party;
- iv) In Adv. Pro. No. 02-2007 Count III of the Plaintiff's complaint was dismissed without prejudice and without costs to any party;
- v) In Adv. Pro. No. 02-2007 Count II of the Plaintiff's complaint was remanded to Cumberland County Superior Court, without costs and attorneys fees to any party. In consenting to remand, Lynch agreed that it would not challenge the subject matter jurisdiction of the Cumberland County Superior Court to conduct the trial and would not attempt to remove or otherwise invoke the jurisdiction of the federal court (except for appellate review to the extent permitted under applicable law), so long as the Plaintiff does not amend the complaint. Now Plaintiff's case will proceed against Lynch in Cumberland County Superior Court in Maine on the issue of whether Lynch has liability to Plaintiffs under the Maine Severance Pay Act. Lynch believes that, in addition to other defenses, it is not subject to the Maine Severance Pay Act, as now in effect, and will move for summary judgment. Management firmly believes that, under current law, the resolution of this case will not have a material adverse effect on the Registrant's consolidated financial condition or operations. Lynch has, however, become aware that plaintiff's counsel is sponsoring legislation to amend the Maine Severance Pay Act that, if enacted, could conceivably adversely affect the outcome of this case. At this time, management is unable to assess the prospects for enactment of any such legislation or, if enacted, how it might affect the outcome of this case.

**2. Spinnaker Chapter 11 Reorganization Proceeding**

On November 13, 2001 (the "Filing Date"), Spinnaker and its Spinnaker Coating, Spinnaker Coating-Maine, Inc. and Entoleter subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States

Bankruptcy Code (11 U.S.C. §101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the “Court”). The cases are being jointly administered under Case No. 01-38066.

Effective December 28, 2001, Spinnaker’s Common Stock and Class A Common Stock were de-listed from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligation to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the “Letter of Intent”) with WR Capital Partners, LLC (“WR Capital”) whereby SP Acquisition LLC (“SP Acquisition”), an acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker’s (and its subsidiaries’) assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations). Entoleter’s assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement (as amended, the “Asset Purchase Agreement”) with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker’s assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker’s equity holders.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter’s assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 5, 2002. If the sale closes, Spinnaker estimates that pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter’s sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (i) and (ii), liquidate Entoleter’s assets.

### **3. Qui Tam Lawsuit**

Lynch Interactive Corporation (“Interactive”), Registrant and several other parties have been named as defendants in a lawsuit brought under the so-called “qui tam” provisions of the federal False Claims Act in the United States District Court for the District of Columbia. The complaint was filed under seal with the court on February 14, 2001. At the initiative of one of the defendants, the seal was lifted on January 11, 2002. Under the False Claims Act, a private plaintiff, termed a “relator,” may file a civil action on the U.S. government’s behalf against another party for violation of the statute. In return, the relator receives a statutory bounty from the government’s litigation proceeds if he is successful.

The relator in this lawsuit is R.C. Taylor III. The main allegation in the case is that the defendants participated in the creation of “sham” bidding entities that allegedly defrauded the federal Treasury by improperly participating in certain Federal Communications Commission spectrum auctions restricted to small businesses, as well as obtaining bidding credits in other spectrum auctions allocated to “small” and “very small” businesses. The lawsuit seeks to recover an unspecified amount of damages, which would be subject to mandatory trebling under the statute.

The U.S. Department of Justice has notified the court that it has declined to intervene in the case. The defendants strongly believe that this lawsuit is completely without merit and intend to defend the suit vigorously. Furthermore, Registrant believes that, under the separation agreement between Registrant and Interactive pursuant to which Interactive was spun off to Registrant’s shareholders on September 1, 1999, Interactive would be obligated to indemnify Registrant for any losses or damages incurred by Registrant as a result of this lawsuit. Nevertheless, Registrant cannot predict the ultimate outcome of the litigation, nor can

Registrant predict the effect that the lawsuit or its outcome will have on Registrant's business or plan of operation. The defendants have yet to be formally served with the complaint.

**Item 4. *Submission of Matters to a Vote of Security Holders***

Not applicable.

**PART II**

**Item 5. *Market for the Registrant's Common Equity and Related Stockholder Matters***

The Common Stock of Lynch Corporation is traded on the American Stock Exchange under the symbol "LGL." The market price highs and lows in consolidated trading of the Common Stock during the two years ended December 31, 2001 and 2000 are as follows:

<u>2001</u>	<u>Three Months Ended</u>			
	<u>March 31</u>	<u>June 30</u>	<u>September 30</u>	<u>December 31</u>
High .....	42	30	34 <sup>9</sup> / <sub>8</sub>	23
Low .....	29	26	23	13
<u>2000</u>	<u>March 31</u>	<u>June 30</u>	<u>September 30</u>	<u>December 31</u>
High .....	33 <sup>1</sup> / <sub>2</sub>	32 <sup>7</sup> / <sub>8</sub>	51	50
Low .....	25 <sup>1</sup> / <sub>4</sub>	25 <sup>1</sup> / <sub>2</sub>	31 <sup>7</sup> / <sub>8</sub>	43

At March 15, 2002, the Company had 836 shareholders of record.

**Compliance with Listing Standards**

On December 11, 2001 AMEX advised Lynch that it was initiating an informal review of Lynch's eligibility for continued listing on AMEX because, based upon AMEX's review of Lynch's Form 10-Q for the period ended September 30, 2001: (1) Lynch had shareholders equity of less than \$2 million and losses from continuing operations in two of its three most recent fiscal years and (2) Lynch had shareholders equity of less than \$4 million and losses in three out of its four most recent fiscal years. AMEX requested Lynch to provide the Exchange with Lynch's specific plan for achieving compliance with the Exchange's continued listing guidelines. On January 10, 2002, Lynch responded to the Exchange, explaining that Lynch's failure to meet the continued listing guidelines was attributable to the fact that, until September 30, 2001, by virtue of its control position in Spinnaker, Lynch was required to consolidate 100% of Spinnaker's losses and that, in the absence of these losses from Spinnaker, Lynch would have reported positive equity and positive net income for the 9-month period ending September 30, 2001. Lynch further explained that its new management team had taken steps to deconsolidate Spinnaker from Lynch for financial reporting purposes effective from and after September 30, 2001 by reducing Lynch's equity and voting interests in Spinnaker below 50%. See "Item 1. Business — C. Spinnaker — Deconsolidation". Lynch explained that the deconsolidation of Spinnaker resulted in a non-cash gain of \$27.4 million being recorded on September 30, 2001 and also resulted in Lynch retaining a negative investment in Spinnaker of \$19.4 million, representing Lynch's remaining interest in Spinnaker's accumulated deficit as of September 30, 2001; that this remaining interest represents losses in excess of investment, which has been recorded as a "deferred gain" on Lynch's balance sheet until such time as Spinnaker achieves profitability or Lynch disposes of its remaining interest in Spinnaker (see Note 1 to the Registrant's Consolidated Financial Statements included in this report); that Lynch will not record any additional losses from Spinnaker; that, in Lynch's view, the \$19.4 million "deferred gain" should be treated as equity by AMEX for purposes of assessing Lynch's compliance with the listing standards; and that, after giving effect to the deconsolidation of Spinnaker, Lynch retains a strong balance sheet. Finally, Lynch explained that management expects Lynch's business will be profitable and that the current negative equity position of Lynch, even before consideration of the aforementioned deferred gain as additional equity, would be reduced annually and turn positive in fiscal 2004.

On January 29, 2002, the Exchange notified Lynch that it had determined to continue Lynch's listing pending a review of its March 31, 2002 Form 10-Q. The Exchange noted that, by then, Lynch should have made favorable progress towards regaining compliance with the listing guidelines. The Exchange further noted that its determination to continue Lynch's listing is subject to Lynch's favorable progress in satisfying the Exchange's guidelines for continued listing and to the Exchange's routine periodic reviews of Lynch's SEC filings. Finally, the Exchange requested a report on or before May 30, 2002 which provides (i) quarterly income statement, cash flow and balance sheet projections for the year ending December 31, 2002; (ii) a copy of Lynch's most recent business plan, if available; and (iii) an update on Lynch's stance with respect to its ownership position in Spinnaker.

The subsequent event described in Note 17 to the Consolidated Financial Statements should have a positive effect on Lynch's eligibility for continued listing.

#### **Dividend Policy**

The Board of Directors has adopted a policy of not paying cash dividends, a policy which is reviewed annually. This policy takes into account the long term growth objectives of the Company, especially its acquisition program, shareholders' desire for capital appreciation of their holdings and the current tax law disincentives for corporate dividend distributions. Accordingly, no cash dividends have been paid since January 30, 1989 and none are expected to be paid in 2002. Substantially all of the subsidiaries' assets are restricted under the companies' current credit agreements and limit the companies' ability to pay dividends.

**Item 6. Selected Financial Data**

**LYNCH CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED SELECTED FINANCIAL DATA**  
**(Adjusted to Reflect Discontinued Operations and Spin Off of Lynch Interactive Corporation)**  
**(In thousands, except per share amounts)**

	Year Ended December 31(a)				
	2001*	2000	1999	1998	1997
Revenues .....	\$141,073	\$219,196	\$194,222	\$187,644	\$153,735
Operating profit (loss) (b) .....	(19,240)	(4,977)	85	4,074	6,730
Net financial activities .....	(7,357)	(12,751)	(9,528)	(8,392)	(4,884)
Gain (loss) on sale of subsidiary stock and other operating assets .....	—	—	—	2,090	(91)
Income (loss) from continuing operations before income Taxes, minority interests, discontinued operations and Extraordinary items.....	(26,597)	(17,728)	(9,443)	(2,228)	1,755
(Provision) benefit for income taxes .....	(358)	2,793	2,544	1,408	(301)
Minority interests .....	4,017	9,252	2,647	1,107	(121)
Income (loss) from continuing operations before Discontinued operations and extraordinary items	(22,938)	(5,683)	(4,252)	287	1,333
Operations of Lynch Interactive Corporation(f) ....	—	—	(7,493)	4,929	(3,349)
Discontinued operations(c) .....	—	—	(572)	(1,859)	(862)
Gain on sale of Spinnaker's industrial tape Segment	—	—	10,431	—	—
Extraordinary items(d) .....	—	2,245	303	—	—
Net income (loss) .....	<u>\$ (22,938)</u>	<u>\$ (3,438)</u>	<u>\$ (1,583)</u>	<u>\$ 3,357</u>	<u>\$ (2,878)</u>
Per Common Share:(e)					
Income (loss) from continuing operations before Discontinued operations and extraordinary items:					
Basic .....	\$ (15.24)	\$ (3.81)	\$ (3.00)	\$ .20	\$ .94
Diluted .....	(15.24)	(3.81)	(3.00)	.20	.94
Net income (loss):					
Basic .....	(15.24)	(2.31)	(1.12)	2.37	(2.03)
Diluted .....	(15.24)	(2.31)	(1.12)	2.37	(2.03)
Cash, securities and short-term investments(g) ....	\$ 4,247	\$ 10,543	\$ 13,106	\$ 1,132	\$ 6,499
Restricted cash(g) (h) .....	4,703	6,500	56,026	—	—
Total assets (net of discontinued operations) (c) (f) (g) .....	32,091	162,820	211,192	251,658	183,720
Long-term debt, exclusive of current portion(g) ....	1,678	61,350	116,765	126,976	115,159
Shareholders' (deficiency) equity(f) (g) .....	(7,451)	15,432	15,991	11,441	14,464

**Notes:**

\* Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

- (a) The data presented herein reflect the spin off of Lynch Interactive Corporation (Interactive) from the Company and the sale by Spinnaker Industries, Inc. (Spinnaker), of its industrial tape units, all of which transactions occurred in the third quarter of 1999. Accordingly, the operating results of both Interactive and the industrial tape segment have been segregated from continuing operations of the Company and are reported as separate line items. The data presented also includes results of the business acquired from S.D. Warren (name changed Spinnaker Coating-Maine, Inc.) from March 17, 1998, the date of its acquisition.
- (b) Operating profit (loss) is revenues less operating expenses, which excludes investment income, interest expense, extraordinary items, minority interests and taxes. Included are asset impairment and restructuring charges and the gain on deconsolidation (see Note g).
- (c) Discontinued operations of the industrial tape segment of Spinnaker Corporation. (See Note 3 to Financial Statements included elsewhere herein).
- (d) Gain on early extinguishments of debt at Spinnaker in 2000 and 1999.
- (e) Based on weighted average number of common shares outstanding.
- (f) No cash dividends have been declared over the period. In 1999 for each share of Lynch Common Stock, shareholders received one share of Lynch Interactive Corporation in a Spin Off of the multimedia and transportation business (See Note 4 to Financial Statements). In 1997, for each share of Lynch Common Stock, shareholders received one share of East/West Communications, Inc., an F block PCS licensee with licenses covering a population of 20 million.
- (g) 2001 excludes Spinnaker Industries as a result of the September 30, 2001 deconsolidation of Spinnaker resulting from the Company's disposition of shares of Spinnaker that reduced its ownership and voting interest of Spinnaker Industries, Inc. to 41.8% and 49.5% respectively.
- (h) See discussion of Restricted Cash in Note 6 — Notes Payable and Long-Term Debt included elsewhere herein.
- (i) For three year trend data of revenues and operating profit (loss) by segment, see Note 15-Segment Information.

**Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations***

**Critical Accounting Policies**

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in Item 8 of this Form 10-K. The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to the carrying value of inventories, realizability of outstanding accounts receivable, percentage of completion of long-term contracts, and the provision for income taxes. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. In the past, actual results have not been materially different from the Company's estimates. However, results may differ from these estimates under different assumptions or conditions.

The Company has identified the following as critical accounting policies, based on the significant judgments and estimates used in determining the amounts reported in its consolidated financial statements:

***Accounts Receivable***

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The Company estimates potential losses based on its knowledge

of the financial condition of certain customers. Historically, losses have been within the Company's expectations. If the financial condition of the Company's customers were to change, adjustments may be required to these estimates.

#### ***Inventory Valuation***

The Company values its inventory at the lower of cost or market. If actual market conditions are more or less favorable than those projected by management, adjustments may be required.

#### ***Accounting for Long-Term Contracts***

One of the Company's subsidiaries is engaged in the manufacture of machines and accounts for the related long-term contracts using the percentage-of-completion accounting method as costs are incurred. Estimates are used to determine the completion percentages and projected profitability of these contracts based on available information. Actual progress made on these contracts may result in future changes to these estimates.

#### ***Income Taxes***

The carrying value of the Company's net deferred tax assets assumes that the Company will be able to generate sufficient future taxable income in certain tax jurisdictions to realize the value of these assets. If the Company is unable to generate sufficient future taxable income in these jurisdictions, an adjustment may be required to the net carrying value of the deferred tax assets resulting in additional income tax expense in the Company's consolidated statement of operations. Management evaluates the realizability of the deferred tax assets and assesses the need for any valuation adjustment quarterly.

#### ***Recently Issued Accounting Standards***

The Company has described the impact anticipated from the adoption of certain new accounting pronouncements effective in 2002 in Note 1 to the consolidated financial statements included elsewhere herein.

### **Results of Operations**

#### ***Year 2001 Compared to 2000 (including Results of Spinnaker for the nine months ended September 30, 2001)***

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and will prospectively account for its ownership of Spinnaker using the equity method of accounting. See Note 1 — "Basis of Presentation" included elsewhere herein. Accordingly, Spinnaker results of operations have only been included for nine months in 2001.

#### ***Net Sales***

Revenues for the year ended December 31, 2001 were \$141.1 million, a reduction of \$78.1 million from Fiscal Year 2000. Spinnaker's net sales for the nine month period ending September 30, 2001 were \$93.4 million, compared to \$155.7 million for the full year in 2000. The decrease in Spinnaker net sales for 2001 was mainly attributable to lower selling prices due to excess capacity and depressed demand caused by the weakened general economy as well as the deconsolidation at September 30, 2001. Another contributing factor was the shutdown of Spinnaker's facility in Maine in the first quarter of 2001.

Lynch Systems' revenues increased by 10 percent to \$26.1 million due to increased order flow and sales of glass press machines used mainly by the producers of television and computer-monitor screens and other devices that incorporate electronic display. M-tron's served market, the infrastructure segment of the telecommunications industry, was deeply depressed by the major correction of overcapacity caused by the



internet bubble. M-tron could not overcome the dramatic reduction in spending by its customers and suffered a sales decline from \$39.8 million in 2000 to \$21.6 million in 2001.

#### *Operating Loss*

Operating loss for 2001 was \$19.2 million compared to an operating loss of \$5.0 million in 2000. Spinnaker's nine-month operating loss was \$47.3 million compared to an operating loss of \$9.5 million in 2000. Spinnaker's operating results primarily reflect lower operating margins due to lower selling prices attributable to excess capacity and a weak general economy. Spinnaker recognized restructuring charges affiliated with its Coating business, during the first nine months of 2001 of \$38.3 million compared to \$2.7 million in 2000. The 2001 restructuring charge was for the closing of the Spinnaker Coating facility in Westbrook, Maine. Non-cash asset impairment charges of \$36.8 million (goodwill \$20.8 million; fixed assets \$16.0 million) accounted for the majority of the \$38.3 million restructuring cost. The Company also recorded a \$27.4 million gain on deconsolidation of Spinnaker as discussed in Note 1 to the consolidated financial statements included elsewhere herein. Subsequent to the Company's deconsolidation of Spinnaker, Spinnaker filed for Chapter 11 bankruptcy protection in November, 2001. As of March 6, 2002, an agreement to sell the majority of the Spinnaker business had been approved by the bankruptcy court. See Note 17 to the consolidated financial statements included elsewhere herein for further details.

M-tron's operating profit declined by \$5.9 million from a profit of \$3.3 million to a loss of \$2.6 million. In spite of a 54 percent reduction in headcount and a further curtailment in hours worked, M-tron could not compensate for the 46 percent reduction in sales and lower selling prices. M-tron's 2000 and 2001 profits were also impacted by IPO/Rights offering costs of \$341,000 and \$266,000, respectively. M-tron's 2001 earnings were also reduced by a product issue with a long time contract manufacturer. M-tron provided reserves for this product issue totaling \$295,000 at December 31, 2001. In addition, M-tron wrote down its inventories by \$675,000 due to the sudden drop in demand that started in March, 2001. Lynch Systems operating profit increased by \$1.9 million to \$4.8 million due to increased order volume and cost controls that enabled Lynch Systems to improve its return on sales by 6 percentage points.

#### *Other Income/Expense*

Investment income decreased by \$1.1 million (all attributable to Spinnaker) caused by lower investment earnings rates, the 9-month versus 12-month comparison, and less cash invested.

Interest expense of \$7.8 million was \$3.6 million less than the prior year primarily due to reduced debt at Lynch Systems, the 9-month versus 12-month comparison at Spinnaker, and lower borrowing rates.

Income tax benefit (expense) includes federal, state and local taxes. In spite of a net loss for the year 2001, there was a \$358,000 tax expense as Spinnaker's loss does not provide any tax benefits to Lynch. Factors resulting in this tax, and factors that reduced the year 2000 effective tax rate to 16% include provisions for contingencies, state income taxes, goodwill amortization, a valuation allowance for deferred taxes, and our foreign sales corporation.

Minority interests, reduced losses by \$4.0 million as a result of losses at Spinnaker that were allocable to the minority interests to the extent of their investment in Spinnaker, and profits of \$0.1 million for the minority interest in Lynch AMAV.

Net loss for the year ended December 31, 2001 was \$22.9 million, or (\$15.24) per share, which compares to the net loss of \$3.4 million, or (\$2.31) per share, for the same period of 2000, and was due primarily to Spinnaker's 9 month loss of \$54.5 million that was partly offset by the \$27.4 million gain on deconsolidation. See Note 1 to the consolidated financial statements included elsewhere herein.

Total backlog of manufactured products at December 31, 2001 (excluding Spinnaker) was \$13.4 million, which represents a decrease of \$12.5 million from the comparable backlog of \$25.9 million at December 31, 2000. Not included in this backlog is \$1.5 million and \$2.2 million at December 31, 2001 and 2000 respectively, representing a payment from a customer for a glass press order at Lynch Systems which was subsequently cancelled. The customer can use this amount for future orders and, if not utilized, will be

forfeited to Lynch Systems. The backlog at Lynch Systems declined slightly from \$13.5 million to \$12.0 million. Meanwhile, the backlog at M-tron decreased to \$1.4 million from \$12.4 million due to the dramatic reduction in buying by OEM suppliers to the telecommunications sector which started in March, 2001.

### *Year 2000 Compared to 1999*

#### *Net Sales*

Revenues for the year ended December 31, 2000 were \$219.2 million, an increase of \$25.0 million from the comparable 1999 period. Spinnaker's 2000 net sales were \$155.7 million, compared to \$162.1 million in 1999. The decrease in net sales for 2000 is attributed to entering into a joint venture to outsource the manufacturing and sales of non-pressure sensitive product lines in the fourth quarter of 1999 and lower sales volumes of general purpose pressure-sensitive products. Net sales were also impacted by lower prices from intense price competition in the general purpose and other pressure-sensitive product lines. Offsetting these declines were increased sales of pressure-sensitive sheet products.

Additionally, net sales at Spinnaker's Entoleter business declined by \$1.4 million due to continued lower unit pricing. Revenues at M-tron increased by \$13.4 million due to increased demand from the telecommunications industry and increased sales of new products. Lynch Systems' revenues increased by \$18.0 million due to increased order flow and sales of glass press machines.

#### *Operating Loss*

Operating loss for 2000 was \$5.0 million compared to an operating profit of \$.1 million in 1999. Spinnaker's operating loss was \$9.5 million compared to operating profit of \$1.6 million in 1999. Spinnaker's operating results primarily reflect lower operating margins, increased depreciation and amortization associated with capital expenditures used in the manufacturing process, lower product volumes, and an increase in product development costs. Spinnaker recognized certain restructuring charges, affiliated with its Coating business, during the fourth quarter 2000 of approximately \$2.2 million and had previously recorded approximately \$.5 million in the first quarter of 2000. To better concentrate on Coating's strengths and market niche, the decision was made by Spinnaker management to reorganize and realign the business in the fourth quarter of 2000 and going forward in 2001. The restructuring involved the elimination of product lines and related manufacturing operations, outsourcing of non-core manufacturing processes and the termination of seven salaried employees, primarily senior management.

M-tron's operating profit increased by \$1.4 million to \$3.3 million due to increased volume and increased margins. Lynch Systems operating profit increased by \$4.9 million to \$2.7 million due to increased order volume and a significant increase in margins over 1999 depressed levels.

#### *Other Income/Expense*

Investment income decreased by \$.6 million due to the utilization of restricted cash from the 1999 sale of Spinnaker's industrial tape units to buy back debt which reduced the funds available for short-term investments.

Interest expense was \$11.4 million and decreased by \$.4 million from the prior year primarily due to the reduction of Spinnaker's Senior Notes by the repurchase mentioned above, offset by interest costs for short-term borrowings at various subsidiaries.

In addition, Spinnaker recognized an impairment loss of \$2.8 million in its investment in certain warrants as a result of the decline during the third and fourth quarter of 2000 in the underlying value of the stock associated with such warrants.

The income tax benefit includes federal, as well as state and local taxes. The tax benefit for the year ended December 31, 2000, and 1999, represents effective tax rates of 16% for 2000 and 27% for 1999. The

differences from the federal statutory rate are principally due to the effect of state income taxes, foreign sales amortization of non-deductible goodwill and a valuation allowance on Spinnaker's deferred tax assets.

Minority interests contribution to the net income (loss) increased by \$6.6 million for the year from the prior year due to the increased losses from continuing operations at Spinnaker.

Net loss for the year ended December 31, 2000, was \$3.4 million, or (\$2.31) per share, which compares to the net loss of \$1.6 million, or (\$1.12) per share, for the same period of 1999, due primarily to the operating losses mentioned above, offset by Spinnaker's gain on repurchase of its Senior Notes (\$2.2 million after income taxes and minority interest).

#### **Liquidity and Capital Resources (Excluding Spinnaker Industries)**

The discussion below excludes the impact of Spinnaker, which was deconsolidated at September 30, 2001 as discussed in Note 1 to the consolidated financial statements included elsewhere herein. Thus, the discussion below reflects liquidity and capital resource matters for the Company's remaining consolidated subsidiaries at December 31, 2001.

At December 31, 2001, the Company had current assets of \$25.9 million and current liabilities of \$16.3 million. Working capital was therefore \$9.6 million as compared to \$9.2 million at December 31, 2000. The ratio of current assets to current liabilities was 1.59 to 1.00 at December 31, 2001, an improvement over the 1.42 to 1.00 ratio at December 31, 2000.

Cash provided by operating activities was approximately \$8.4 million in 2001 compared to cash used of approximately \$2.9 million in 2000.

Capital expenditures, on a comparable basis, were \$0.6 million in 2001 and \$1.6 million in 2000. Capital expenditures in 2002 may return to the 2000 level of \$1.6 million. The Company anticipates that it will have sufficient cash flow from operations and borrowing availability under various credit facilities at the subsidiaries to fund such capital expenditures.

At December 31, 2001, total debt was \$3.3 million, which was \$2.3 million less than the \$5.6 million outstanding at the end of 2000. The reduction in debt is primarily due to reductions in the revolving credit loans. Debt outstanding at December 31, 2001 included \$940 thousand of fixed interest rate debt, at an 8.0% interest rate, and \$2.3 million of variable interest rate debt at a year end 2001 average rate of 5.0%. In May of 2001, Lynch Systems entered into an agreement with a bank for a \$4 million line of credit to be used only for the issuance of standby letters of credit. This line of credit is secured by accounts receivable and inventories. Amounts available under this line of credit will be used to fund letters of credit securing customer advances and certain warranty coverages. In August of 2001, M-tron entered into a credit agreement with its bank to set the line at \$6.2 million, including a \$5.0 million working capital line. In addition, the company has aggregate lease commitments of \$786,000. (See Note 14 to the Consolidated Financial Statements).

Lynch Systems has a February 2002 commitment from another bank to provide a \$6 million export/import line, a \$2 million domestic revolving credit line, and a \$944 thousand term loan. Interest rates will be variable and currently would average about 4.6 percent. All of the new lenders' loan conditions have been met and the lender expects to close the loan by mid-April 2002. In the event the new loan is not closed, Lynch Systems would pursue other alternatives that could include funding by its parent, renewing the present bank line, and entering into a lending agreement with another financing source.

In 1987, the Board of Directors of Lynch authorized the repurchase of 400,000 common shares. As of December 31, 2001, Lynch's remaining authorization is to repurchase an additional 148,700 shares of common stock. On August 9, 2001, the Company purchased 12,300 shares of its Common Stock from a former director, Mr. Guzzetti, for a purchase price of \$396,204. Such purchase price was equal to the outstanding principal amount and unpaid interest on the loans made by the Company to Mr. Guzzetti on June 5, 2000 and September 20, 2000 to finance his original purchase of such Common Stock.

The Board of Directors has adopted a policy of not paying cash dividends, a policy which is reviewed annually. This policy takes into account the long term growth objectives of the Company, especially its

acquisition program, shareholders' desire for capital appreciation of their holdings and the current tax law disincentives for corporate dividend distributions. Accordingly, no cash dividends have been paid since January 30, 1989 and none are expected to be paid in 2002. (See Note 6 to the Consolidated Financial Statements for restrictions on the companies assets).

### **Market Risk**

The Company is exposed to market risk relating to changes in the general level of U.S. interest rates. Changes in interest rates affect the amounts of interest earned on the Company's cash equivalents and short-term investments (approximately \$8.9 million at December 31, 2001). The Company generally finances the debt portion of the acquisition of long-term assets with fixed rate, long-term debt. The Company generally maintains the majority of its debt as fixed rate in nature by borrowing on a fixed long-term basis. The Company does not use derivative financial instruments for trading or speculative purposes. Management does not foresee any significant changes in the strategies used to manage interest rate risk in the near future, although the strategies may be reevaluated as market conditions dictate. There has been no significant change in market risk since December 31, 2001.

At December 31, 2001, approximately \$2.3 million of the Company's debt bears interest at variable rates. Accordingly, the Company's earnings and cash flows are slightly affected by changes in interest rates. Assuming the current level of borrowings for variable rate debt, and assuming a two percentage point increase in the 2001 average interest rate under these borrowings, it is estimated that the Company's interest expense would change by only \$0.1 million. In the event of an adverse change in interest rates, management would take actions to further mitigate its exposure.

### **Concentrations of Credit Risk**

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, investments, and trade accounts receivable.

The Company maintains cash and cash equivalents and short investments with various financial institutions. These financial institutions are located throughout the country and the Company's policy is designed to limit exposure to any one institution. The Company performs periodic evaluations of the relative credit standing of those financial institutions that are considered in the Company's investment strategy. Other than certain accounts receivable, the Company does not require collateral on these financial instruments. In relation to export sales, the Company requires letters of credit supporting a significant portion of the sales price prior to production to limit exposure to credit risk. The Company maintains an allowance for doubtful accounts at a level that management believes is sufficient to cover potential credit losses.

### **Risk Factors**

Certain subsidiaries and business segments of the Company sell to industries that are subject to cyclical economic changes. Any downturns in the economic environment would have a financial impact on the Company and its consolidated subsidiaries and may cause the reported financial information herein not to be indicative of future operating results, financial condition or cash flows.

Future activities and operating results may be adversely affected by fluctuating demand for capital goods such as large glass presses, delay in the recovery of demand for components used by telecommunications infrastructure manufacturers, disruption of foreign economies and the inability to renew or obtain new financing for expiring loans.

### **Item 7A. *Quantitative and Qualitative Disclosure About Market Risk***

The information required by this Item 7A is included under the caption "Market Risk" in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7.

**Item 8. *Financial Statements and Supplementary Data***

See Item 14(a).

**Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

Not applicable.

**PART III**

**Item 10. *Directors and Executive Officers of the Registrant***

The information required by this Item 10 is included under the caption “Executive Officers of the Registrant” in Item 1 hereof and included under the captions “Election of Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is incorporated herein by reference.

**Item 11. *Executive Compensation***

The information required by this Item 11 is included under the captions “Compensation of Directors,” “Executive Compensation,” “Executive Compensation and Benefits Committee Report on Executive Compensation” and “Performance Graph” in Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is incorporated herein by reference.

**Item 12. *Security Ownership of Certain Beneficial Owners and Management***

The information required by this Item 12 is included under the caption “Security Ownership of Certain Beneficial Owners and Management,” in the Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is included herein by reference.

**Item 13. *Certain Relationships and Related Transactions***

The information required by this Item 13 is included under the caption “Executive Compensation”, and “Transactions with Certain Affiliated Persons” in the Registrant’s Proxy Statement for its Annual Meeting of Shareholders for 2002, which information is included herein by reference.

**PART IV**

**Item 14. *Exhibits, Financial Statements, Financial Statement Schedules and Reports on Form 8-K***

(a) The following documents are filed as part of this Form 10-K Annual Report:

(1) Financial Statements:

The Report of Independent Auditors and the following Consolidated Financial Statements of the Company are included herein:

Consolidated Balance Sheets at December 31, 2001 and 2000

Consolidated Statements of Operations — Years ended December 31, 2001, 2000 and 1999

Consolidated Statements of Shareholders’ Equity — Years ended December 31, 2001, 2000, and 1999

Consolidated Statements of Cash Flows — Years ended December 31, 2001, 2000, and 1999

Notes to Consolidated Financial Statements

(2) Financial Statement Schedules as of December 31, 2001 and 2000 and for the three years ended December 31, 2001:

Schedule I — Condensed Financial Information of Registrant

Schedule II — Valuation and Qualifying Accounts

All other schedules for which provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions, or are inapplicable, and therefore have been omitted.

See Page 2 above re Forward Looking Information.

(b) Reports on Form 8-K: None

(c) The following Exhibits listed in the Exhibit Index are filed with this Form 10-K Annual Report:

2(a) — Asset Purchase Agreement (“Asset Purchase Agreement”), dated January 18, 2002, by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and SP Acquisition, LLC.

2(b) — Asset Purchase Agreement Amendment No. 1 dated February 15, 2002.

2(c) — Asset Purchase Agreement Amendment No. 2 dated February 25, 2002.

2(d) — Asset Purchase Agreement Amendment No. 3 dated March 5, 2002.

2(e) — Asset Purchase Agreement Amendment No. 4 dated March 8, 2002.

2(f) — Asset Purchase Agreement Amendment No. 5 dated March 18, 2002.

2(g) — Schedules to Asset Purchase Agreement dated January 18, 2002.

2(h) — United States Bankruptcy Court Order dated March 6, 2002; In Re: Spinnaker Industries, Inc., et al., C.A. No. 01-38066.

10(x) — Amendment dated February 7, 2002 among Registrant, Mario J. Gabelli and Ralph R. Papitto, amending the Agreement at Exhibit 10(w) to terminate Registrant’s obligation to grant an option to Mr. Papitto.

10(y) — Registrant’s 2001 Equity Incentive Plan adopted December 10, 2001.

21 — Subsidiaries of the Registrant.

23 — Consent of Ernst & Young LLP.

24 — Powers of Attorney.

(d) Financial Statement Schedules:

Financial Statement Schedules are listed in response to Item 14(a)(2)

## REPORT OF INDEPENDENT AUDITORS

Shareholders and Board of Directors  
Lynch Corporation

We have audited the accompanying consolidated balance sheets of Lynch Corporation and subsidiaries (“Lynch Corporation” or the “Company”) as of December 31, 2001 and 2000, and the related consolidated statements of operations, shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2001. Our audits also included the financial statement schedules listed in the index at Item 14(a). These financial statements and schedules are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lynch Corporation and subsidiaries at December 31, 2001 and 2000 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statements schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects, the information set forth therein.

/s/ ERNST & YOUNG LLP

Stamford, Connecticut  
March 29, 2002

**LYNCH CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**

	<b>December 31, 2001</b>	<b>December 31, 2000</b>
	<b>(In thousands, except share amounts)</b>	
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents .....	\$ 4,247	\$ 10,543
Restricted cash (Note 1) .....	4,703	6,500
Trade accounts receivable, less allowances of \$118 and \$1,582, respectively .....	9,818	35,019
Inventories .....	5,260	35,139
Deferred income taxes .....	988	7,624
Prepaid expense .....	836	1,807
Total Current Assets .....	25,852	96,632
Property, Plant and Equipment		
Land .....	291	797
Buildings and improvements .....	4,158	11,076
Machinery and equipment .....	11,949	56,951
	16,398	68,824
Less: Accumulated depreciation .....	(10,942)	(27,713)
	5,456	41,111
Excess of cost over fair value of net assets acquired, net. ....	—	21,589
Other assets .....	537	3,488
Total Assets .....	\$ 31,845	\$162,820
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Notes payable to banks .....	\$ 1,086	\$ 30,288
Trade accounts payable .....	1,717	19,251
Accrued interest payable .....	7	1,185
Accrued liabilities .....	6,189	15,234
Customer advances .....	6,781	3,916
Current maturities of long-term debt .....	521	1,376
Total Current Liabilities .....	16,301	71,250
Long-term debt .....	1,678	61,350
Deferred income taxes .....	578	6,752
Other long-term liabilities .....	1,319	3,908
Minority interests .....	—	4,128
Total Liabilities .....	19,876	147,388
Loss in Excess of Investment (Note 1) .....	19,420	—
Comments and Contingencies (Note 14)		
Shareholders' (Deficiency) Equity		
Common stock, no par or stated value — 10,000,000 shares Authorized; 1,513,191 shares issued; 1,497,883 and 1,510,183 shares outstanding .....	5,139	5,139
Additional paid-in capital .....	10,403	10,403
(Accumulated deficit) retained earnings .....	(22,533)	405
Officer's note receivable .....	—	(382)
Accumulated other comprehensive loss .....	(2)	(71)
Treasury stock of 15,308 and 3,008 shares at cost .....	(458)	(62)
Total Shareholders' (Deficiency) Equity .....	(7,451)	15,432
Total Liabilities and Shareholders' (Deficiency) Equity .....	\$ 31,845	\$162,820

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.



**LYNCH CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

	Years ended December 31,		
	2001	2000	1999
	(In thousands, except share and per-share amounts)		
SALES AND REVENUES.....	\$ 141,073	\$ 219,196	\$ 194,222
Costs and expenses:			
Manufacturing cost of sales .....	130,290	192,980	172,567
Selling and administrative .....	19,157	28,485	21,120
Asset impairment and restructuring charges .....	38,272	2,708	450
	187,719	224,173	194,137
Gain on deconsolidation (Note 1) .....	27,406	—	—
OPERATING PROFIT (LOSS) .....	(19,240)	(4,977)	85
Other income (expense):			
Investment income .....	384	1,481	2,354
Interest expense .....	(7,741)	(11,432)	(11,882)
Impairment of Spinnaker's investment in warrants .....	—	(2,800)	—
	(7,357)	(12,751)	(9,528)
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES, MINORITY INTERESTS, DISCONTINUED OPERATIONS AND EXTRAORDINARY ITEM .....	(26,597)	(17,728)	(9,443)
(Provision) Benefit for income taxes .....	(358)	2,793	2,544
Minority interests .....	4,017	9,252	2,647
LOSS FROM CONTINUING OPERATIONS BEFORE DISCONTINUED OPERATIONS AND EXTRAORDINARY ITEM ..	(22,938)	(5,683)	(4,252)
DISCONTINUED OPERATIONS:			
Loss from operations of Lynch Interactive Corporation distributed to shareholders (less income tax benefit of \$3,068 and minority interests of \$578) .....	—	—	(7,493)
Loss from discontinued operations of industrial tape segment of Spinnaker Industries (less applicable income tax benefit of \$308 and minority interests of \$558) .....	—	—	(572)
Gain on sale of Spinnaker's industrial tape operations (less income tax provision of \$6,495 and minority interest of \$7,013) .....	—	—	10,431
EXTRAORDINARY ITEM:			
Gain on early extinguishments of debt (less income tax provision of \$2,612 and \$355 and minority interest of \$2,472 and \$300) .....	—	2,245	303
NET LOSS .....	\$ (22,938)	\$ (3,438)	\$ (1,583)
Weighted average shares outstanding .....	1,505,300	1,491,000	1,415,000
Basic and diluted loss per share:			
Loss from continuing operations before discontinued operations .....	\$ (15.24)	\$ (3.81)	\$ (3.00)
Loss from Lynch Interactive Corporation .....	—	—	(5.30)
Income from discontinued operations .....	—	—	6.97
Extraordinary item .....	—	1.51	.21
NET LOSS .....	\$ (15.24)	\$ (2.30)	\$ (1.12)

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

*See accompanying notes*

**LYNCH CORPORATION AND SUBSIDIARIES**  
**Consolidated Statements of Shareholders' Equity**  
**For the Three Years Ended December 31, 2001**

	Shares of Common Stock Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Officer's Note Receivable	Accumulated Other Comprehensive Income	Treasury Stock	Total
	(In thousands except for shares of common stock)							
BALANCE AT DEC. 31, 1998 . . . . .	1,418,248	5,139	8,554	26,771	\$ 0	59	(730)	39,793
Comprehensive Income (Loss):								
Net loss for year . . . . .	—	—	—	(1,583)	—	—	—	(1,583)
Other comprehensive income (loss) . . . . .	—	—	—	—	—	(40)	—	(40)
Comprehensive Income (Loss) . . . . .								(1,623)
Purchase of Treasury Stock . . . . .	(8,065)	—	—	—	—	—	(523)	(523)
Capital transactions of The Morgan Group, Inc. . . . .	—	—	(252)	—	—	—	—	(252)
Dividend of Lynch Interactive Corporation . . . . .	—	—	—	(21,345)	—	(59)	—	(21,404)
BALANCE AT DEC. 31, 1999 . . . . .	1,410,183	5,139	8,302	3,843	\$ 0	(40)	(1,253)	15,991
Comprehensive Income (Loss):								
Net loss for year . . . . .	—	—	—	(3,438)	—	—	—	(3,438)
Other comprehensive income (loss) . . . . .	—	—	—	—	—	(31)	—	(31)
Comprehensive Income (Loss) . . . . .								(3,469)
Issuance of Common Stock . . . . .	100,000	—	1,809	—	—	—	1,191	3,000
Capital transactions of Lynch Systems	—	—	292	—	—	—	—	292
Loan to Officer to buy Common stock	—	—	—	—	(382)	—	—	(382)
BALANCE AT DEC. 31, 2000 . . . . .	1,510,183	\$5,139	\$10,403	\$ 405	(\$ 382)	\$ (71)	\$ (62)	\$15,432
Comprehensive Income (Loss):								
Net loss for year . . . . .	—	—	—	(22,938)	—	—	—	(22,938)
Other comprehensive income . . . . .	—	—	—	—	—	69	—	69
Comprehensive Income (Loss) . . . . .								(22,869)
Acquisition of Treasury Stock . . . . .	(12,300)	—	—	—	382	—	(396)	(14)
BALANCE AT DEC. 31, 2001 . . . . .	<u>1,497,883</u>	<u>\$5,139</u>	<u>\$10,403</u>	<u>\$(22,533)</u>	<u>\$ —</u>	<u>\$ (2)</u>	<u>(458)</u>	<u>\$(7,451)</u>

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

*See accompanying notes.*

**LYNCH CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Years Ended December 31,</b>		
	<b>2001</b>	<b>2000</b>	<b>1999</b>
	(In thousands)		
<b>OPERATING ACTIVITIES</b>			
Net loss .....	\$(22,938)	\$ (3,438)	\$ (1,583)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities of continuing operations:			
Gain on deconsolidation .....	(27,406)	—	—
Loss on donation of shares .....	366	—	—
Asset impairment and restructuring charges .....	38,272	—	—
Extraordinary item, net .....	—	(2,245)	(303)
Depreciation .....	4,315	6,734	5,147
Amortization of goodwill and other assets .....	244	1,001	1,087
Amortization of deferred financing charges .....	703	876	786
Deferred taxes .....	501	1,846	(2,719)
Minority interests .....	(4,017)	(7,072)	(2,636)
Other .....	761	2,800	(854)
Adjustment from discontinued operations:			
Loss from operations of Lynch Interactive Corporation .....	—	—	7,493
Loss from operations of industrial tape segment .....	—	—	572
Gain on sale of industrial tape segment .....	—	—	(10,431)
Changes in operating assets and liabilities:			
Receivables .....	10,861	(10,377)	678
Inventories .....	13,430	(3,459)	(3,284)
Accounts payable and accrued liabilities .....	(14,269)	10,112	(3,949)
Other Assets/Liabilities .....	4,727	(212)	864
Net cash provided by (used in) operating activities of continuing operations .....	5,550	(3,434)	(9,132)
<b>INVESTING ACTIVITIES</b>			
Capital Expenditures .....	(1,104)	(4,323)	(3,795)
Restricted Cash .....	1,797	49,526	(56,026)
Reduction in cash due to deconsolidation .....	(5,728)	—	—
Proceeds from sale of industrial tape segment .....	—	—	104,450
Proceeds from sale of fixed assets .....	—	—	2,403
Other .....	(860)	(767)	509
Net cash provided by (used in) investing activities of continuing operations .....	(5,895)	44,436	47,541
<b>FINANCING ACTIVITIES</b>			
Net borrowings (repayments) of notes payable .....	(7,587)	7,110	(36,127)
Repayment of long-term debt .....	(420)	(53,433)	(10,937)
Proceeds from long-term debt .....	1,987	—	—
(Purchase) sale of treasury stock .....	—	1,191	(523)
Issuance of common stock .....	—	1,809	—
Other .....	69	(242)	(580)
Net cash used in financing activities of continuing operations .....	(5,951)	(43,565)	(48,167)
Net decrease in cash and cash equivalents .....	(6,296)	(2,563)	(9,758)
Cash provided by Lynch Interactive Corporation .....	—	—	15,987
Cash provided by industrial tape segment .....	—	—	5,745
Increase (decrease) in cash and cash equivalents .....	(6,296)	(2,563)	11,974
Cash and cash equivalents at beginning of year .....	10,543	13,106	1,132
Cash and cash equivalents at end of year .....	\$ 4,247	\$ 10,543	\$ 13,106

Effective September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1.

*See accompanying notes*

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**December 31, 2001**

**1. Accounting and Reporting Policies**

*Organization*

Lynch Corporation is a diversified holding company with subsidiaries engaged in manufacturing primarily in the United States. The Company has two wholly-owned subsidiaries (Lynch Systems, Inc. and M-tron Industries, Inc.) and an investment in Spinnaker Industries, Inc. (“Spinnaker”) accounted for under the equity method of accounting; see discussion below. Information on the Company’s operations by segment and geographic area is included in Note 15 — Segment Information.

*Basis of Presentation*

Prior to September 30, 2001, the Company owned 47.6% of the equity of Spinnaker (60.4% voting control), an entity engaged in the manufacture of adhesive-backed material; as such, under accounting principles generally accepted in the United States, Spinnaker was a consolidated entity and the Company was required to record all of the losses of Spinnaker since the non-Company interests were not required to absorb their share of the losses (52.4%) after their investment was fully absorbed by losses (which occurred in the first quarter of 2001).

Effective September 30, 2001, the Company donated 430,000 shares of Spinnaker Class A common stock to a university on whose board several of the Company’s executives serve as Trustees, thereby relinquishing control of such securities. This resulted in the reduction of the Company’s ownership and voting interests in Spinnaker to 41.8% and 49.5%, respectively. As a result, effective September 30, 2001, the Company deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting.

Accordingly, the Company’s results of operations include the operating results of Spinnaker through September 30, 2001 (date of deconsolidation). The balance sheet at December 31, 2001 does not contain the assets and liabilities of Spinnaker due to the deconsolidation. This deconsolidation resulted in a non-cash gain of \$27,406,000 being recorded on September 30, 2001 to reduce the Company’s negative investment in Spinnaker to \$19,420,000, which represents the Company’s interest in Spinnaker’s accumulated deficit at the date of deconsolidation. This remaining interest represents losses in excess of investment, which has been recorded as a deferred credit on the Company’s balance sheet until such time as Spinnaker achieves profitability or the Company disposes of its remaining interests in Spinnaker. The Company will not record any additional losses from Spinnaker as the Company has no further obligations to Spinnaker (see Note 17).

The following summarized balance sheet information of Spinnaker is presented as follows at September 30, 2001 (date of deconsolidation) and December 31, 2000):

	<u>(unaudited)</u> <u>September 30,</u> <u>2001</u>	<u>December 31,</u> <u>2000</u>
Current Assets .....	\$ 36,881	\$ 59,496
Total Assets .....	54,902	119,031
Current Liabilities .....	38,759	49,409
Long-Term Debt .....	61,239	60,310
Shareholder’s Deficit .....	(46,460)	(7,468)

*Principles of Consolidation*

The consolidated financial statements include the accounts of Lynch Corporation (the “Company” or “Lynch”) and entities in which Lynch had majority voting control. All material intercompany transactions

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

and accounts have been eliminated in consolidation. See Note 4 for details of the spin off of Lynch Interactive Corporation, which occurred on September 1, 1999.

*Uses of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

*Cash Equivalents*

Cash equivalents consist of highly liquid investments with a maturity of less than three months when purchased.

At December 31, 2001 and 2000, assets of \$2.1 million and \$8.7 million, which are classified as cash and cash equivalents, are invested in United States Treasury money market funds for which affiliates of the Company serve as investment managers to the respective funds.

*Restricted Cash*

At December 31, 2001 and 2000, the Company had \$4.7 million and \$6.5 million of Restricted Cash. (See Note 6.)

*Accounts Receivable*

Accounts receivable on a consolidated basis consist principally of amounts due from both domestic and foreign customers. Credit is extended based on an evaluation of the customer's financial condition and collateral is not generally required except at Lynch Systems (See discussion of Accounting for Long Term Contracts below). The Company considers concentrations of credit risk to be minimal due to the Company's diverse customer base. In relation to export sales, the Company requires letters of credit supporting a significant portion of the sales price prior to production to limit exposure to credit risk. Certain subsidiaries and business segments have credit sales to industries that are subject to cyclical economic changes. The Company maintains an allowance for doubtful accounts at a level that management believes is sufficient to cover potential credit losses.

*Property, Plant and Equipment, Net*

Property, plant and equipment are recorded at cost less accumulated depreciation and include expenditures for additions and major improvements. Maintenance and repairs are charged to operations as incurred. Depreciation is computed for financial reporting purposes using the straight-line method over the estimated useful lives of the assets, which range from 5 years to 35 years for buildings and for 3 to 10 years for other fixed assets. For income tax purposes, accelerated depreciation methods are used.

*Excess of Cost over Fair Value of Net Assets Acquired, Net*

As of December 31, 2001, there is no goodwill on the books of Lynch Corporation. The majority of goodwill on Spinnaker books at December 31, 2000 (\$20.8 million) was written-off in 2001 and is included in asset impairment and restructuring charges in the statements of operations (See Note 2).

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

***Revenue Recognition***

Revenues, with the exception of certain long-term contracts discussed below, are recognized on shipment. Shipping costs are included in manufacturing cost of sales.

***Accounting for Long-Term Contracts***

Lynch Systems, a 100% owned subsidiary of the Company, is engaged in the manufacture and marketing of glass-forming machines and specialized manufacturing machines. Certain sales contracts require an advance payment (usually 30% of the contract price) which is accounted for as a customer advance. The contractual sales prices are paid either (i) as the manufacturing process reaches specified levels of completion or (ii) based on the shipment date. Guarantees by letter of credit from a qualifying financial institution are required for most sales contracts. Because of the specialized nature of these machines and the period of time needed to complete production and shipping, Lynch Systems accounts for these contracts using the percentage-of-completion accounting method as costs are incurred (cost to cost basis). At December 31, 2001 and 2000, costs and estimated earnings in excess of billings (included in accounts receivable) were \$5.3 million and \$2.7 million, respectively.

***Research and Development Costs***

Research and development costs are charged to operations as incurred. Such costs were \$1,772,000, \$1,603,000, and \$1,386,000 in 2001, 2000, and 1999, respectively.

***Advertising Expense***

The cost of advertising is expensed as incurred. The Company incurred \$177,000, \$472,000, and \$340,000 in advertising costs during 2001, 2000 and 1999, respectively.

***Earnings Per Share***

The Company's basic and diluted earnings per share are equivalent as the Company has no dilutive securities (see Note 9).

***Segment Information***

The Company reports segment information in accordance with Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information" (SFAS 131). SFAS No. 131 requires companies to report financial and descriptive information for each operating segment based on management's internal organizational decision-making structure. See Note 15 for the detailed presentation of business segments report.

***Impairments***

The Company accounts for impairments of long-lived assets in accordance with the provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Assets to be Disposed Of". The Company periodically assesses the net realizable value of its long-lived assets and evaluates such assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. For assets to be held and used, impairment is determined to exist if estimated undiscounted future cash flows are less than the carrying amount. For assets to be disposed of, impairment is determined to exist if the estimated net realizable value is less than the carrying amount. If indicators of impairment are present, and we do not expect the estimated undiscounted cash flows to be derived from the related assets to be sufficient to recover the asset's carrying amount, an impairment loss is charged to expense in the period identified based upon the difference between the carrying amount and the discounted cash flows. The rates

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

that would be utilized to discount the net cash flows to net present value would take into account the time value of money and investment risk factors. See Note 2 regarding Spinnaker's restructuring costs for fiscal years 2001 and 2000.

***Stock Based Compensation***

The Company grants stock options for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant. The Company accounts for stock option grants in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25) and related Interpretations because the Company believes the alternative fair value accounting provided for under FASB Statement No. 123, *Accounting for Stock-Based Compensation*, (FAS 123) requires the use of option valuation models that were not developed for use in valuing employee stock options.

***Financial Instruments***

Cash and cash equivalents, trade accounts receivable, short-term borrowings, trade accounts payable and accrued liabilities are carried at cost which approximates fair value due to the short-term maturity of these instruments. The carrying account of the Company's borrowings under its revolving lines of credit approximates fair value, as the obligations bear interest at a floating rate. The fair value of other long-term obligations approximates cost based on borrowing rates for similar instruments.

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, investments, trade accounts receivable.

The Company maintains cash and cash equivalents and short-term investments with various financial institutions. These financial institutions are located throughout the country and the Company's policy is designed to limit exposure to any one institution. The Company performs periodic evaluations of the relative credit standing of those financial institutions that are considered in the Company's investment strategy. Other than certain accounts receivable, the Company does not require collateral on these financial instruments.

***Issuance of Stock by Subsidiaries and Investees***

Changes in the Company's equity in a subsidiary or an investee caused by issuance of the subsidiary's or investees' stock are accounted for as gains or losses where such issuance is not part of a broader reorganization (see Note 10).

***Reclassifications***

The consolidated financial statements reflect the spin off of Lynch Interactive Corporation (Interactive) from Lynch Corporation that occurred in the third quarter of 1999 and also the sale by Spinnaker Industries, Inc. (Spinnaker), of its two industrial tape units, Central Products Company and Spinnaker Electrical that also occurred in the third quarter of 1999.

Accordingly, the operating results of both Interactive and the industrial tape segment have been segregated from continuing operations of the Company and are reported as separate line items on the financial statements as discontinued operations.

Certain other amounts in the 2000 and 1999 financial statements have been reclassified to conform to the 2001 presentation. These other reclassifications are immaterial to the consolidated financial statements taken as a whole.

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

***Recent Issued Accounting Pronouncements***

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 141, “Business Combinations” (“FAS 141”), and Statement of Financial Accounting Standards No. 142, “Goodwill and Other Intangible Assets” (“FAS 142”). FAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. FAS 141 also includes guidance on the initial recognition and measurement of goodwill and intangible assets arising from business combinations completed after June 30, 2001. FAS 142 requires that these assets be reviewed for impairment at least annually. Intangible assets with finite lives will continue to be amortized over their estimated useful lives. Additionally, FAS 142 requires that goodwill included in the carrying value of equity method investments no longer be amortized.

The Company will apply FAS 142 beginning in the first quarter of 2002. The Company will test indefinite-lived intangible assets for impairment using the two-step process prescribed by FAS 142. The first step is a screen for potential impairment, while the second step measures the amount of impairment, if any. The Company expects to perform the first of the required impairment tests of indefinite-lived intangible assets as of January 1, 2002 in the first quarter of 2002. Any impairment charge resulting from these transitional impairment tests will be reflected as the cumulative effect of a change in accounting principles in the first quarter of 2002. The Company does not anticipate that the effect of these tests will be material to the earnings and financial position of the Company.

In August 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets” (“FAS 144”), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes Statement of Financial Accounting Standards No. 121, “Accounting for the Impairment of Long-Lived Assets to be Disposed Of”, and the accounting and reporting provisions of APB Opinion No. 30, “Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequent Occurring Events and Transactions”. FAS 144 is effective for fiscal years beginning after December 15, 2001. The Company will adopt FAS 144 as of January 1, 2002 and it does not expect that the adoption of the Statement will have a significant impact on the Company’s financial position or results of operations.

**2. Asset Impairment and Restructuring Charges**

Prior to the deconsolidation of Spinnaker on September 30, 2001 (see Note 1), the Company recognized certain restructuring charges in 2001 related to Spinnaker, totaling \$41.8 million. The charges resulted from (a) the write-down to estimated fair market value of fixed assets to be taken out of service and held for sale or disposal; (b) impairment of goodwill associated with the acquisition of Coating — Maine in 1998; (c) severance and related costs; and (d) inventory write-downs of \$3.5 million (recorded through manufacturing costs of sales).

To better concentrate on Coating’s strengths and market niche, a decision was made by Spinnaker’s management to reorganize and realign the business in the fourth quarter of 2000. Spinnaker recognized certain restructuring charges, primarily affiliated with its Spinnaker Coating and Spinnaker Coating — Maine businesses, in 2000 of approximately \$2.7 million.

**3. Discontinued Operations**

On April 9, 1999, Spinnaker entered into a definitive agreement to sell its industrial tape segment to Intertape Polymer Group, Inc. for approximately \$105 million and five-year warrants to purchase 300,000 shares of Intertape common stock (New York Stock Exchange Symbol “ITP”) at an exercise price of \$29.50 per share. At the time, the warrants were valued at approximately \$3.0 million using the Black-Scholes option



**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

pricing model. At December 31, 2000, the fair value of the warrants was approximately \$0.2 million, accordingly, in accordance with SFAS No. 121, Spinnaker recognized an impairment loss of \$2.8 million as a result of the decline during the third and fourth quarters of 2000 in the market value of the stock associated with the warrants which are recorded in other assets.

The sale of the two industrial tape businesses closed on August 10, 1999 and July 30, 1999. Accordingly, operating results of the industrial tape segment have been segregated from continuing operations and reported as a separate line item in the statements of operations. The Company recorded gains totaling \$17.4 million, net of applicable income taxes of approximately \$6.5 million. Spinnaker offset the cash tax liability by utilizing net operating loss carry forwards. The industrial tape segments net sales were \$69.5 million in the period ended December 31, 1999 (through the date of sale).

General corporate office expenses related to finance and administrative functions including public company compliance reporting, bank and investor relations, taxes other than income taxes and holding company payroll, historically allocated and charged to the industrial tape segment were reversed and allocated back to continuing operations. These expenses were not considered to be directly attributed to discontinued operations. Historical expenses allocated back to continuing operations totaled \$1.0 million for the period ended December 31, 1999.

Interest expense attributed to the Spinnaker senior notes and related deferred financing had historically been allocated based on the pro rata share of subsidiary debt obligations retired with the proceeds from the issuance of the senior notes, to total debt obligations retired. The senior note proceeds were used to extinguish certain outstanding term and revolver obligations in October 1996. Interest expense charged to the discontinued industrial tape segment totaled \$5.2 million for the period ended December 31, 1999.

#### **4. Spin Off**

On August 12, 1999, the Board of Directors approved a plan to distribute the stock of Lynch Interactive Corporation on a one for one basis to the shareholders of Lynch Corporation (“spin off”). Lynch completed the spin off of Lynch Interactive Corporation (“Interactive”) on September 1, 1999, to stockholders of record on August 23, 1999. Pursuant to the spin off, each Lynch shareholder received one share of Interactive common stock for each share of Lynch owned. Lynch had received a private letter ruling from the Internal Revenue Service that the spin off would be tax free to Lynch shareholders. Interactive is listed on the American Stock Exchange under the symbol “LIC”.

Interactive owns all of what were Lynch’s multimedia and service businesses while Lynch retained the manufacturing businesses. Interactive owns the telephone companies, television interests and PCS interests, as well as the 55% equity interest of The Morgan Group, Inc. In addition, Interactive owns a 13.6% equity interest in Spinnaker Industries, Inc. In the third quarter of 1999, Lynch acquired by merger, all of the stock of Central Scott Telephone Company. This company became part of Lynch Interactive and was included in the spin off.

As a result, the Company’s multimedia and services segments are being reported as operations distributed to shareholders in the accompanying consolidated financial statements. Accordingly, operating results of Lynch Interactive Corporation for 1999 have been segregated from continuing operations and reported as a separate line item on the statements of operations. Interactive’s net sales were \$ 204.6 million for the fiscal year ended December 31, 1999.

Lynch Interactive and Lynch have entered into certain agreements governing various ongoing relationships, including the provision of support services and a tax allocation agreement. The tax allocation agreement provides for the allocation of tax attributes to each company as if it had actually filed with the respective tax authority. At the spin off, the employees of the corporate office of Lynch Corporation became the employees of Lynch Interactive Corporation and Lynch Interactive Corporation began providing certain support services

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to Lynch. The Company was charged a management fee for these services amounting to approximately \$180,000, \$265,000 and \$200,000 in 2001, 2000 and 1999, respectively. Note that this arrangement was terminated in August, 2001.

The net assets distributed to Interactive were estimated to be \$22.6 million at September 1, 1999. Such amount was subsequently decreased in the fourth quarter by \$1.6 million to reflect revised estimates of liabilities distributed.

**5. Inventories**

Inventories are stated at the lower of cost or market value. Inventories valued using the last-in, first-out (LIFO) method comprised approximately 20% (which excluded Spinnaker due to the deconsolidation discussed in Note 1) and 28% of consolidated inventories at December 31, 2001 and 2000, respectively. The balance of inventories at December 31, 2001 are valued using the first-in-first-out (FIFO) method. At December 31, 2000, the balance of inventories were valued using the FIFO method and specific identification method (for Spinnaker).

	December 31,	
	2001	2000
	(In Thousands)	
Raw materials and supplies .....	\$1,844	\$10,172
Work in progress .....	2,003	2,796
Finished goods .....	1,413	22,171
Total .....	\$5,260	\$35,139

Current cost exceeded the LIFO value of inventories by \$991,000 and \$966,000 at December 31, 2001 and 2000, respectively.

**6. Notes Payable to Banks and Long-term Debt**

Notes payable to banks and long-term debt consists of:

	December 31,	
	2001	2000
	(In Thousands)	
Notes payable:		
M-tron bank revolving loan at variable interest rates (4.5% at December 31, 2001), due May 2002 .....	\$1,086	\$ 3,004
Lynch Systems bank revolving loan at variable interest rates, due August 2002 .....	—	1,150
Spinnaker notes payable with variable interest rates .....	—	26,134
	\$1,086	\$30,288
Long-term debt:		
M-tron term loan at variable interest rates (5.0% at December 31, 2001), due September 2004 .....	\$1,259	\$ —
Lynch Systems term loan at a fixed interest rate of 8.0%, due August 2003 .....	607	635
Spinnaker 10.75% senior secured notes, due 2006 .....	—	51,135
Spinnaker subordinated note at a fixed interest rate of 14%, due 2003 .....	—	9,172
Other debt .....	333	1,784
	2,199	62,726
Current maturities .....	(521)	(1,376)
	\$1,678	\$61,350

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

On a consolidated basis, at December 31, 2001, Lynch maintains short-term and long-term line of credit facilities totaling \$10.2 million, of which \$5.9 million was available for future borrowings. These facilities generally limit the credit available under the lines of credit to certain variables, such as inventories and receivables, and are secured by the operating assets of the respective subsidiary borrower, and include various financial covenants which currently restrict the transfer of substantially all the assets of the subsidiaries. At December 31, 2001, all of these facilities expire within one year. The weighted average interest rate for short-term borrowings at December 31, 2001 and 2000 was 5.0% and 9.5%, respectively. In May of 2001, Lynch Systems entered into an agreement with a bank for a \$4 million line of credit to be used only for the issuance of standby letters of credit. This line of credit is secured by accounts receivable and inventories. Amounts available under this line of credit will be used to fund letters of credit securing customer advances and certain warranty coverages. Cash of \$4.7 million at December 31, 2001 has been disclosed as restricted as required under certain letters of credit outstanding. Total letters of credit outstanding at December 31, 2001 totaled \$7.9 million. In August of 2001, M-tron entered into a credit agreement with its bank to set the line at \$6.2 million including a \$5.0 million working capital line. Lynch Systems has a February 2002 commitment from another bank to provide a \$6 million export/import line, a \$2 million domestic revolving credit line, and a \$944 thousand term loan. Interest rates will be variable and would currently average about 4.6 percent. All of the new lender's loan conditions have been met and the lender expects to close the loan by mid-April 2002. This new financing will be used to repay the existing Lynch Systems debt.

Cash payments for interest were \$2.0 million, \$10.4 million, and \$10.3 million for the years ended December 31, 2001, 2000 and 1999, respectively. Interest payments in 2001 are substantially below 2000 due to Spinnaker's defaulting on interest payments.

Aggregate principal maturities of long-term debt (excluding Spinnaker) for each of the next five years that total 2.1 million are as follows: 2002 — \$521 thousand; 2003 — \$816 thousand; 2004 — \$863 thousand; and 0 thereafter.

**7. Minority Interests and Related Party Transactions**

Pursuant to a subscription agreement entered into on March 11, 2000, the Company sold 100,000 shares of its Common Stock to Mario J. Gabelli, Chairman of the Company at that time and current Vice-Chairman of the Company, for \$30 per share, in cash, or \$3 million in total, which represented a premium of 14.6% above the closing price of \$26.125 per share of the stock on the American Stock Exchange on March 9, 2000, the date said sale was authorized by the Board of Directors.

The sale was exempt from registration under the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof. The proceeds were available for general corporate purposes, including possible acquisitions. The sale was ratified by the shareholders of the Company at its Annual Meeting held on May 11, 2000.

***Transactions with Certain Affiliated Persons***

Mr. Gabelli is affiliated with various entities which he directly or indirectly controls and which are engaged in various aspects of the securities business. During 2001, the Company and its subsidiaries engaged in various transactions with certain of these entities and the amount of commissions, fees, and other remunerations paid to such entities, excluding reimbursement of certain expenses related to Mr. Gabelli's employment by the Corporation, was not material.

On October 1, 2001, the Company transferred its' principal executive offices to Providence, Rhode Island from Rye, New York. These offices are shared with Avtek, Inc. ("Avtek") a private holding company co-owned by Mr. Papitto (Company Chairman) and Mr. Gabelli. Since August 2001, Avtek and the Company have shared, on an approximately equal basis, (i) all occupancy costs of the shared premises and

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(ii) the salary expense of certain persons employed by Avtek at the premises (including Mr. McGrail, the Company's President and Chief Operating Officer and Mr. Keller, the Company's Chief Financial Officer, and other administrative and clerical personnel) whose services are provided to both the Company and Avtek. The Company's share of such occupancy and salary costs in 2001 was \$73,000, a portion of which represents compensation to Mr. McGrail and Mr. Keller that is reported in the Summary Compensation Table of the Proxy Statement which was paid subsequent to December 31, 2001.

In the opinion of management, the method of allocating these costs was reasonable; however, the costs of these services allocated to the Company are not necessarily indicative of the costs that would have been included on a stand alone basis.

***Equity Transactions***

Effective July 31, 2001, Louis A. Guzzetti, Jr. resigned from the Board of Directors of the Company. In connection with Mr. Guzzetti's resignation, on August 9, 2001, the Company purchased 12,300 shares of its Common Stock for its treasury from Mr. Guzzetti for a purchase price of \$396,204. Such purchase price was equal to the outstanding principal amount and unpaid interest on the loans made by the Company to Mr. Guzzetti on June 5, 2000 and September 20, 2000 to finance his original purchase of such Common Stock.

Mr. Gabelli's loan to the Company in the amount of \$371,000 to fund the loan to Mr. Guzzetti, which was issued in September, 2000 at an initial interest rate of 7.5% per annum adjusted prospectively on each interest payment date to two points below the prime rate, was repaid to Mr. Gabelli by the Company on August 10, 2001.

**8. Spinnaker Chapter 11 Reorganization Proceeding**

On November 13, 2001 (the "Filing Date"), Spinnaker and its Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and Entoleter, Inc. subsidiaries filed voluntary petitions for relief under chapter 11 of the United States Bankruptcy Code (11 U.S.C. & 101 et. al.) in the United States Bankruptcy Court for the Southern District of Ohio, Dayton Division (the "Court"). The cases are being jointly administered under Case No. 01-38066. Effective December 28, 2001, Spinnaker's Common Stock and Class A Common Stock were de-listed from the American Stock Exchange. Spinnaker has also filed a Form 15 with the Securities and Exchange Commission to terminate its obligations to file periodic reports under the Securities Exchange Act of 1934.

On December 31, 2001, Spinnaker entered into a letter of intent (the "Letter of Intent") with WR Capital Partners, LLC ("WR Capital") whereby SP Acquisition LLC ("SP Acquisition"), and acquisition entity established by WR Capital, agreed to purchase substantially all of Spinnaker's (and its subsidiaries') assets (and assumption of substantial liabilities) for an amount not to exceed \$25,763,000 (including assumed obligations), subject to adjustment. Entoleter's assets are not included in the sale. On January 4, 2002, Spinnaker filed a motion with the Court to approve the sale of substantially all of its assets, subject to higher and better offers, to SP Acquisition. On January 17, 2002, the Court entered an order (i) approving bid procedures, including a break-up fee and expense reimbursement, (ii) setting an auction date of March 4, 2002 and (iii) setting a date to issue an order approving the sale of such assets for March 5, 2002.

On January 18, 2002, Spinnaker entered into that certain Asset Purchase Agreement ("the Asset Purchase Agreement") with SP Acquisition as contemplated by the Letter of Intent. On March 6, 2002, the Court entered an order approving the sale of substantially all of Spinnaker's assets to SP Acquisition.

The closing of the Asset Purchase Agreement occurred on March 28, 2002. Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to

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Spinnaker's equity holders. As a result, management believes that the Company's investment in Spinnaker is worthless.

On March 28, 2002, the Court approved the sale of substantially all of Entoleter's assets to Welton LLC for \$920,000 in cash plus certain assumed obligations. The closing of the sale is expected to occur on or before April 15, 2002. If the sale closes, Spinnaker estimates that, pursuant to a plan of liquidation, there will be a minimal distribution to unsecured creditors and no return to Spinnaker, Entoleter's sole equity holder. If the sale does not close, Spinnaker may, among other actions, (i) search for another purchaser of Entoleter, (ii) attempt to cause Entoleter to reorganize pursuant to a plan of reorganization, or (iii) if unsuccessful with respect to (i) and (ii), liquidate Entoleter's assets. (See Note 17).

**9. Stock Option Plans**

On December 10, 2001, the Board of Directors approved, subject to shareholder approval at the May 2002 Annual Meeting, the 2001 Equity Incentive Plan and the issuance of up to 300,000 options to purchase shares of Company common stock to certain employees of the Company, of which 228,000 options were granted (subject to shareholder approval) at \$17.50 per share on December 10, 2001. As the grants required shareholder approval, they are not considered issued until the approval is received. As a result, the Company may be required to record a non-cash charge associated with these options if the market price of the Company's stock exceeds \$17.50 at the approval date. If approved, 180,000 of these options would be fully vested, with the remaining options vesting quarterly over the next three years.

Spinnaker has two plans (Directors' and Stock Incentive Plans) under which stock options for the purchase of common shares can be granted. Total options outstanding under these plans were 82,000 and 92,000 at weighted average exercise prices of \$21.53 and \$24.95 per share at December 31, 2000 and 1999, respectively. At December 31, 2000, 44,669 options were exercisable. These options are not presented at December 31, 2001 due to the deconsolidation of Spinnaker (see Note 1).

The pro forma effect on the Company's operations, under the disclosure requirements of FAS 123 was net loss of \$3,464,000 and \$2,832,000 and basic and diluted loss per share of (\$2.32) and (\$2.00) in 2000 and 1999, respectively. The fair value of each option grant was estimated using the Black-Scholes option-pricing model, assuring 50% volatility, 6% risk-free interest rates, a 3-year expected option life and no dividends. No FAS 123 disclosure has been provided for 2001 as such amounts are not materially different from reported results.

**10. Shareholders' Equity**

The Board of Directors has authorized the purchase of up to 400,000 shares of Common Stock. Through December 31, 2000, 238,991 shares had been purchased at an average cost of \$14.88 per share.

On February 1, 1996, the Company adopted a plan to provide a portion of the compensation for its directors in common shares of the Company. The amount of common stock is based upon the market price at the end of the previous year. Through December 31, 2001, a total of 4,126 shares have been awarded under this program. No stock was issued for compensation during 2001, 2000 and 1999.

Both M-tron and Lynch Systems have plans that provided certain former shareholders with Stock Appreciation Rights (SAR's). These SAR's are fully vested and expire at the earlier of certain defined events or 2008 to 2010. These SAR's provide the participants a certain percentage, ranging from 1-5%, of the increase in the defined value of M-tron and Lynch Systems, respectively. Vested amounts are payable at the holder's option in cash or equivalent amount of M-tron or Lynch Systems stock. Expense related to the SAR's was \$195,000 in 2001, \$145,000 in 2000, and \$62,000 in 1999. At December 31, 2001 and 2000 \$402,000 and \$207,000 respectively are accrued for the SARs.

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Subsequent to the spin off of Interactive in 1999, the Company, with the concurrence of the holders of all outstanding Stock Appreciation Rights units, terminated its Stock Appreciation Rights program for corporate management, including all outstanding units, thus eliminating possible future profit and loss and cash flow distortions associated with the program. As a result of the termination, the Company recorded approximately \$700,000 of related corporate expense in the fourth quarter of 1999.

**11. Income Taxes**

The Company files consolidated federal income tax returns which include all subsidiaries including Interactive through the date of the spin off in 1999, but excluding Spinnaker for all periods.

Deferred income taxes for 2001 and 2000 are provided for the temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities. Cumulative temporary differences and carry-forwards at December 31, 2001 and 2000 are as follows:

	<u>December 31, 2001</u>		<u>December 31, 2000</u>	
	<u>Deferred Tax</u>	<u>Deferred Tax</u>	<u>Deferred Tax</u>	<u>Deferred Tax</u>
	<u>Asset</u>	<u>Liability</u>	<u>Asset</u>	<u>Liability</u>
	(In Thousands)			
Inventory reserve . . . . .	\$ 744	\$ —	\$ 465	\$ —
Fixed assets written up under Purchase accounting and tax over book depreciation . . . . .	—	499	—	5,249
Basis difference in subsidiary and affiliate Stock . . . . .	—	—	—	1,105
Net operating losses of Subsidiaries . . . . .	—	—	6,027	—
Other reserves and accruals . . . . .	1,215	—	4,268	—
Other . . . . .	—	1,050	—	398
Capital loss and other carry forwards . . . . .	<u>938</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total deferred income taxes . . . . .	2,897	<u>1,549</u>	10,760	<u>\$6,752</u>
Valuation allowance . . . . .	<u>(938)</u>	<u>—</u>	<u>(3,136)</u>	<u>—</u>
	<u>\$1,959</u>	<u>—</u>	<u>\$ 7,624</u>	<u>—</u>

At December 31, 2001, Lynch Corporation had capital loss carry-forwards that are fully offset by a valuation allowance of \$938,000. At December 31, 2000, Spinnaker had federal and state net operating loss carry-forwards. For financial reporting purposes, a valuation allowance of \$3.1 million was recognized to offset the deferred tax assets related to those carry-forwards.

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The provision (benefit) for income taxes from continuing operations is summarized as follows:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Current:			
Federal .....	\$(439)	\$ 136	\$ (158)
State and local .....	<u>274</u>	<u>—</u>	<u>—</u>
Foreign .....	<u>22</u>	<u>—</u>	<u>—</u>
Total Current .....	<u>(143)</u>	<u>136</u>	<u>(158)</u>
Deferred:			
Federal .....	489	(2,731)	(2,386)
State and local .....	<u>12</u>	<u>(198)</u>	<u>—</u>
Total Deferred .....	<u>501</u>	<u>(2,929)</u>	<u>(2,386)</u>
	<u>\$ 358</u>	<u>\$(2,793)</u>	<u>\$(2,544)</u>

A reconciliation of the provision (benefit) for income taxes from continuing operations and the amount computed by applying the statutory federal income tax rate to income before income taxes, minority interest and extraordinary item:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Tax (benefit) at statutory rate .....	\$ (9,043)	\$(6,028)	\$(3,211)
State and local taxes, net of federal benefit .....	189	(130)	—
Amortization of goodwill .....	—	111	60
Operating losses of subsidiaries .....	—	—	164
Provision for contingencies .....	—	—	338
Spinnaker operating loss .....	18,533	—	—
Deconsolidation gain .....	(10,132)	—	—
Foreign Sales Corporation .....	(236)	(199)	—
Valuation allowance .....	938	3,136	—
Other .....	<u>109</u>	<u>317</u>	<u>105</u>
	<u>\$ 358</u>	<u>\$(2,793)</u>	<u>\$(2,544)</u>

Gain (loss) before income taxes from foreign operations was \$671,000, (\$313,000) and (\$579,000) in 2001, 2000, and 1999 respectively.

Income tax payments were \$1.2 million, \$1.3 million, and \$1.2 million for the years 2001, 2000 and 1999, respectively.

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**12. Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss, net of related tax, at December 31, 2001, 2000, and 1999 are as follows:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Balance beginning of year . . . . .	\$(71)	\$(40)	\$ 59
Foreign currency translation . . . . .	69	(31)	(40)
Distribution to Lynch Interactive Corporation . . . . .	<u>—</u>	<u>—</u>	<u>(59)</u>
Accumulated other comprehensive loss . . . . .	<u>\$ (2)</u>	<u>\$ (71)</u>	<u>\$ (40)</u>

**13. Employee Benefit Plans**

The Company, through its operating subsidiaries, has several and various employee retirement type plans including defined benefit, defined contribution, multi-employer, profit sharing, and 401 (k) plans. The following table sets forth the consolidated expenses (including Spinnaker's expenses through September 30, 2001) for these plans:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Defined contribution:			
Lynch Systems & M-tron . . . . .	\$ 17	\$ 38	\$ 19
Spinnaker . . . . .	346	335	542
Defined benefit (Spinnaker) . . . . .	202	98	166
Multi-employer (Spinnaker) . . . . .	<u>42</u>	<u>88</u>	<u>121</u>
Total . . . . .	<u>\$607</u>	<u>\$559</u>	<u>\$848</u>

Under the Lynch Systems and M-tron defined contribution plan, the Company contributes up to a maximum of 25 percent of participants contributions that do not exceed \$800 per participant in the plan year. The Company contribution occurs at the end of the plan year and the participant is immediately vested in the employers' contribution.

Spinnaker and its subsidiaries have several defined benefit plans (both Union and non-Union). At December 31, 2000, total benefit obligations for these plans were \$2.4 million. The assumptions used in determining the obligations included average discount rates of 8.0%, an average compensation increases of 0 to 4% and average long-term rate of return on plan assets of 8%. Total plan assets were \$2.0 million at December 31, 2000. Spinnaker also has a defined contribution plan for substantially all employees, under which Spinnaker can match up to 50% of employee contributions not exceeding 8% of compensation. No disclosure was made for 2001 due to the deconsolidation of Spinnaker (see Note 1).

**14. Commitments and Contingencies**

In the normal course of business, subsidiaries of the Company are defendants in certain product liability, worker claims and other litigation in which the amounts being sought may exceed insurance coverage levels. The resolution of these matters is not expected to have a material effect on the Company's financial condition or operations.

The Company, Lynch Interactive Corporation ("Interactive"), and several other parties have been named as defendants in a lawsuit brought under the so-called "qui tam" provisions of the federal False Claims Act in the United States District Court for the District of Columbia. Although the complaint was filed under



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seal with the court on February 14, 2001, and the seal was lifted on January 11, 2002, the defendants have yet to be formally served with the complaint. The main allegation in the case is that the defendants participated in the creation of “sham” bidding entities that allegedly defrauded the federal Treasury by improperly participating in certain Federal Communications Commission spectrum auctions restricted to small businesses, as well as obtaining bidding credits in other spectrum auctions allocated to “small” and “very small” businesses. The lawsuit seeks to recover an unspecified amount of damages, which would be subject to mandatory trebling under the statute.

The U.S. Department of Justice has notified the court that it has declined to intervene in the case. The defendants strongly believe that this lawsuit is completely without merit and intend to defend the suit vigorously. Furthermore, the Company believes that, under the separation agreement between the Company and Interactive pursuant to which Interactive was spun-off to the Company’s shareholders on September 1, 1999, Interactive would be obligated to indemnify the Company for any losses or damages incurred by the Company as a result of this lawsuit.

Rent expense under operating leases was \$846,000 (including Spinnaker for nine months), \$1,213,000, and \$1,222,000 for the years ended December 31, 2001, 2000 and 1999, respectively. The Company leases certain property and equipment, including warehousing and sales and distribution equipment, under operating leases that extend from one to five years. Certain of these leases have renewal options and escalation provisions.

Future minimum rental payments under long-term non-cancelable operating leases for the five years subsequent to December 31, 2001 are as follows (in thousands):

2002.....	\$303
2003.....	167
2004.....	156
2005.....	108
2006.....	52
Thereafter.....	<u>0</u>
	<u>\$786</u>

**15. Segment Information**

The Company has four reportable business segments. The largest is Spinnaker Coating’s adhesive backed label stock for labels and related applications. The second largest segment is Lynch Systems glass manufacturing equipment business. Frequency control devices (quartz crystals and oscillators) manufactured and sold by M-tron is the third segment. Entoleter (subsidiary of Spinnaker Industries, Inc.) manufactures and sells industrial process equipment and is the fourth segment. Spinnaker Coating and Entoleter results for 2001 represent the nine-month period ending September 30, 2001 pursuant to the “deconsolidation” of Spinnaker on September 30, 2001 (see Note 1). Each of the businesses is located domestically and consolidated export sales (primarily Canada and China) were approximately \$38.3 million in 2001, \$54.7 million in 2000, and \$31.5 million in 1999. For the year ended December 31, 2001, one customer accounted for \$5.6 million or 24.5 percent of Lynch Systems’ sales while one customer represented \$2.9 million or 13.5% of frequency control sales. The Company considers concentrations of credit risk to be minimal due to its diverse customer base and because it requires letters of credit of most foreign customers to support a significant portion of the purchase price.

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M-tron attempts to utilize standard parts and components that are available from multiple vendors located in the United States or internationally; however, some components used in its products are available from only a limited number of sources.

EBITDA (before corporate allocation) for operating segments is equal to operating profit before depreciation, amortization and allocated corporate expenses. EBITDA is presented because it is a widely accepted financial indicator of value and ability to incur and service debt. EBITDA is not a substitute for operating income or cash flows from operating activities in accordance with generally accepted accounting principles.

Operating profit (loss) is equal to revenues less operating expenses, excluding unallocated general corporate expenses, interest and income taxes. The Company allocates a portion of its general corporate expenses to its operating segments. Such allocation was \$289,000 in 2001 and \$300,000 per year in 2000 and 1999. Identifiable assets of each industry segment are the assets used by the segment in its operations excluding general corporate assets. General corporate assets are principally cash and cash equivalents, short-term investments and certain other investments and receivables.

	<u>Years ended December 31</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
<b>Revenues</b>			
Adhesive-backed label stock .....	\$ 90,163	\$150,136	\$155,112
Glass manufacturing equipment .....	26,047	23,608	5,656
Frequency control devices .....	21,593	39,855	26,484
Industrial process equipment .....	<u>3,270</u>	<u>5,597</u>	<u>6,970</u>
Consolidated total .....	<u>\$141,073</u>	<u>\$219,196</u>	<u>\$194,222</u>
<b>EBITDA (before corporation allocation)</b>			
Adhesive-backed label stock .....	\$ (4,755)	\$ 99	\$ 8,940
Glass manufacturing equipment .....	5,125	3,239	(1,766)
Frequency control devices .....	(1,770)	4,054	2,540
Industrial process equipment .....	77	440	473
Corporate manufacturing expenses .....	<u>(1,140)</u>	<u>(1,973)</u>	<u>(1,930)</u>
Total manufacturing .....	(2,463)	5,859	8,257
Corporate expenses, net .....	(985)	(1,451)	(1,152)
Restructuring charge — Spinnaker .....	<u>(1,520)</u>	<u>(1,650)</u>	<u>—</u>
Consolidated total .....	<u>\$ (4,968)</u>	<u>\$ 2,758</u>	<u>\$ 7,105</u>

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

	<u>Years ended December 31</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
<b>Operating Profit</b>			
Adhesive-backed label stock .....	\$ (7,860)	\$ (5,137)	\$ 4,155
Glass manufacturing equipment .....	4,778	2,867	(2,042)
Frequency control devices .....	(2,549)	3,345	1,900
Industrial process equipment .....	(22)	280	321
Corporate manufacturing expenses .....	<u>(1,065)</u>	<u>(1,873)</u>	<u>(2,794)</u>
Total manufacturing .....	(6,718)	(518)	1,540
Unallocated Corporate expense .....	(1,656)	(1,751)	(1,455)
Gain on deconsolidation .....	27,406	—	—
Restructuring charge — Spinnaker .....	<u>(38,272)</u>	<u>(2,708)</u>	<u>—</u>
Consolidated Total .....	<u>\$ (19,240)</u>	<u>\$ (4,977)</u>	<u>\$ 85</u>
<b>Depreciation and Amortization</b>			
Adhesive-backed label stock .....	\$ 3,105	\$ 5,236	\$ 4,785
Glass manufacturing equipment .....	461	472	376
Frequency control devices .....	879	809	740
Industrial process equipment .....	99	160	152
Corporate manufacturing expenses .....	<u>15</u>	<u>1,058</u>	<u>181</u>
Consolidated Total .....	<u>\$ 4,559</u>	<u>\$ 7,735</u>	<u>\$ 6,234</u>
<b>Capital expenditures</b>			
Adhesive-backed label stock .....	\$ 430	\$ 2,631	\$ 2,625
Glass manufacturing equipment .....	217	183	154
Frequency control devices .....	429	1,476	804
Industrial process equipment .....	<u>28</u>	<u>33</u>	<u>212</u>
Consolidated Total .....	<u>\$ 1,104</u>	<u>\$ 4,323</u>	<u>\$ 3,795</u>
<b>Total Assets</b>			
Adhesive-backed label stock .....	\$ —	\$116,746	\$105,674
Glass manufacturing equipment .....	22,496	17,908	7,695
Frequency control devices .....	7,901	18,210	10,940
Industrial process equipment .....	—	2,285	2,730
General Corporate .....	<u>1,448</u>	<u>7,671</u>	<u>84,153</u>
Consolidated Total .....	<u>\$ 31,845</u>	<u>\$162,820</u>	<u>\$211,192</u>
Total operating profit for reportable segments			
Other profit or loss: .....	\$ (19,240)	\$ (4,977)	\$ 85
Investment income .....	384	1,481	2,354
Interest expense .....	(7,741)	(11,432)	(11,882)
Impairment of Spinnaker's investment in warrants .....	<u>—</u>	<u>(2,800)</u>	<u>—</u>
Income (loss) from continuing operations before income taxes, minority interests and extraordinary items .....	<u>\$ (26,597)</u>	<u>\$ (17,728)</u>	<u>\$ (9,443)</u>

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting (see Note 1).

**16. Quarterly Results of Operations (unaudited)**

The following is a summary of the quarterly results of operations for the years ended December 31, 2001 and December 31, 2000 (in thousands, except per share amounts):

	<b>2001 Three Months Ended</b>			
	<u>Mar. 31</u>	<u>June 30</u>	<u>Sep. 30(b)</u>	<u>Dec. 31(b)</u>
Sales and revenues .....	\$53,548	\$45,353	\$31,982	\$10,190
Gross profit .....	4,995	692	2,661	2,435
Operating profit (loss) (a) .....	(37,093)	(5,870)	24,379	(656)
Net income (loss) .....	(36,070)	(8,673)	23,082	(1,277)
Basic and diluted earnings (loss) per share .....	(23.89)	(5.74)	15.36	(0.85)
	<b>2000 Three Months Ended</b>			
	<u>Mar. 31(c)</u>	<u>June 30(c)</u>	<u>Sep. 30</u>	<u>Dec. 31(d)</u>
Sales and revenues .....	\$52,474	\$53,008	\$56,192	\$57,522
Gross profit .....	6,147	7,560	8,266	4,243
Operating profit (loss) .....	(142)	1,532	508	(6,875)
Income (loss) from continuing operations before extraordinary item .....	(758)	140	226	(5,291)
Net income (loss) .....	496	1,131	226	(5,291)
Basic and diluted earnings (loss) per share:				
Income (loss) from continuing operations before extraordinary item .....	(.53)	0.09	0.15	(3.50)
Net income (loss) .....	.35	0.75	0.15	(3.50)

**NOTE:**

- a) Includes restructuring costs applicable to Spinnaker of: 1st Quarter — \$36,484; 2nd Quarter — \$5,051; 3rd Quarter — \$219 and gain on deconsolidation of \$27,406 in the 3rd Quarter.
- b) Effective September 30, 2001, the Company deconsolidated Spinnaker (see Note 1). As a result, fourth quarter results do not include Spinnaker results.
- c) Includes gain on early extinguishments of debt of \$2.2 million after income taxes and minority interests.
- d) Includes restructuring charge of approximately \$2.2 million, deferred tax asset valuation allowance of \$3.1 million and investment write-down of \$2.8 million all at Spinnaker.

**17. Subsequent Events**

On March 28, 2002, Spinnaker Industries (excluding Entoleter) was acquired by S P Acquisition LLC (an entity of WR Capital Partners LLC) for \$25.8 million. On March 26, 2002, an auction was held with a subsequent hearing on March 28, 2002 for the Bankruptcy Court which approved the sale of Entoleter to Welton, LLC for approximately \$0.9 million plus certain assumed obligations.

**LYNCH CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

In each case, no return to equity holders is anticipated. Therefore, as a result, the Company anticipates eliminating its remaining interest in Spinnaker and its subsidiaries upon conclusion of the bankruptcy proceedings expected to occur in the second quarter of 2002. At that time, the \$19,420,000 “loss in excess of investment” on the Company’s December 31, 2001 balance sheet will become a non-cash income item and increase shareholders’ equity. If this event would have occurred on December 31, 2001, the Company’s pro-forma equity would have been \$11,969,000, not the reported deficit amount of (\$7,451,000).

**SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF  
REGISTRANT LYNCH CORPORATION**

**CONDENSED BALANCE SHEET**

	<b>2001</b>	<b>2000</b>
	(In Thousands)	
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and Cash Equivalents .....	\$ 2,208	\$ 1,928
Dividend Receivable From Subsidiary .....	—	1,500
Deferred Income Taxes .....	412	412
Other Current Assets .....	76	980
	2,696	4,820
OFFICE EQUIPMENT (Net of depreciation) .....	—	16
OTHER ASSETS (principally investment in and amounts due from wholly owned subsidiaries) .....	10,517	13,057
<b>TOTAL ASSETS</b> .....	<b>\$13,213</b>	<b>\$17,893</b>
<b>LIABILITIES AND SHAREHOLDERS' (DEFICIENCY) EQUITY</b>		
CURRENT LIABILITIES .....	\$ 1,213	\$ 2,303
LONG TERM LIABILITIES .....	31	158
LOSS IN EXCESS OF INVESTMENT .....	19,420	—
<b>TOTAL SHAREHOLDERS' (DEFICIENCY) EQUITY</b> .....	<b>(7,451)</b>	<b>15,432</b>
Total Liabilities and Shareholders' (Deficiency) Equity .....	<b>\$13,213</b>	<b>\$17,893</b>

\* On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

**LYNCH CORPORATION**  
**CONDENSED FINANCIAL INFORMATION OF REGISTRANT**  
**CONDENSED STATEMENT OF OPERATIONS**

	<u>Year Ended December 31</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Interest, Dividends & Gains on Sale of Marketable Securities .....	\$ 209	\$ 187	\$ 17
Dividend from Subsidiary .....	—	1,500	—
Interest & Other Income from Subsidiaries .....	<u>24</u>	<u>348</u>	<u>23</u>
<b>TOTAL INCOME</b> .....	<b>\$ 233</b>	<b>\$ 2,035</b>	<b>40</b>
Costs & Expenses:			
Unallocated Corporate Administrative Expense .....	1,001	1,451	1,155
Interest Expense .....	23	15	7
Interest Expense to Subsidiaries .....	<u>—</u>	<u>—</u>	<u>23</u>
<b>TOTAL COST AND EXPENSE</b> .....	<b><u>1,024</u></b>	<b><u>1,466</u></b>	<b><u>1,185</u></b>
<b>INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY IN NET LOSS OF SUBSIDIARIES</b> .....	<b>(791)</b>	<b>569</b>	<b>(1,145)</b>
Income Tax Benefit (Provision) .....	269	(215)	321
Equity in Net Loss of Subsidiaries .....	<u>(22,416)</u>	<u>(3,792)</u>	<u>(759)</u>
<b>NET LOSS</b> .....	<b><u><u>\$ (22,938)</u></u></b>	<b><u><u>\$ (3,438)</u></u></b>	<b><u><u>\$ (1,583)</u></u></b>

\* On September 30, 2001, the Company's ownership and voting interest of Spinnaker Industries, Inc. was reduced to 41.8% and 49.5% respectively, due to the disposition of shares of Spinnaker. As a result, effective September 30, 2001, the Company relinquished control of Spinnaker and has deconsolidated Spinnaker and prospectively accounts for its ownership of Spinnaker using the equity method of accounting. See Note 1 to Consolidated Financial Statements — "Basis of Presentation" included elsewhere herein.

**LYNCH CORPORATION**  
**CONDENSED FINANCIAL INFORMATION OF REGISTRANT**  
**CONDENSED STATEMENTS OF CASH FLOW**

	<u>Year Ended December 31</u>		
	<u>2001</u>	<u>2000</u>	<u>1999</u>
	(In Thousands)		
Cash provided from (used in) Operating Activities .....	\$(1,220)	\$(2,210)	\$ 405
<b>INVESTING ACTIVITIES:</b>			
Investment in Lynch Manufacturing .....	—	—	981
Dividend from subsidiaries .....	<u>1,500</u>	<u>—</u>	<u>—</u>
<b>NET CASH PROVIDED FROM INVESTING ACTIVITIES .....</b>	<u>1,500</u>	<u>—</u>	<u>981</u>
<b>FINANCING ACTIVITIES:</b>			
(Purchase) Sale of Treasury Stock .....	—	1,191	(523)
Issuance of Common Stock .....	—	1,809	—
Other .....	<u>—</u>	<u>(16)</u>	<u>—</u>
<b>NET CASH (USED IN) PROVIDED FROM FINANCING</b> <b>ACTIVITIES .....</b>	<u>—</u>	<u>2,984</u>	<u>(523)</u>
<b>TOTAL INCREASE IN CASH AND CASH EQUIVALENTS .....</b>	<b>280</b>	<b>774</b>	<b>863</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING</b> <b>OF YEAR .....</b>	<u>1,928</u>	<u>1,154</u>	<u>291</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR .....</b>	<u><u>\$ 2,208</u></u>	<u><u>\$ 1,928</u></u>	<u><u>\$1,154</u></u>

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

***NOTE A — BASIS OF PRESENTATION***

In the parent company's financial statements, the Company's investment in subsidiaries is stated at cost plus equity in undistributed earnings of the subsidiaries.

***NOTE B — SPIN OFF OF LYNCH INTERACTIVE CORPORATION***

On August 12, 1999, the Board of Directors approved a plan to distribute the stock of Lynch Interactive Corporation on a one for one basis to the shareholders of Lynch Corporation ("spin off"). Lynch completed the spin off of Lynch Interactive Corporation ("Interactive") on September 1, 1999, to stockholders of record on August 23, 1999. Pursuant to the spin off, each Lynch shareholder received one share of Interactive common stock for each share of Lynch owned. Lynch had received a private letter ruling from the Internal Revenue Service that the spin off would be tax free to Lynch shareholders. Interactive is listed on the American Stock Exchange under the symbol "LIC".

***NOTE C — DIVIDENDS FROM SUBSIDIARIES***

Dividends paid to Lynch Corporation from the Registrant's consolidated subsidiaries were \$1,500,000 in 2001. No dividends were paid in 2000 and 1999 and no other dividends were received from subsidiaries or investees.



**NOTE D — SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR ADDITIONAL INFORMATION.**

**LYNCH CORPORATION AND SUBSIDIARIES**  
**SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS**  
**YEARS ENDED DECEMBER 31, 2001, 2000 AND 1999**

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>		<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance at Beginning of Period</u>	<u>Additions</u>		<u>Deductions(B)</u>	<u>Balance at End of Period</u>
		<u>Charged to Costs and Expenses</u>	<u>Charged to Other Accounts(A)</u>		
Year ended December 31, 2001					
Allowance for uncollectible .....	<u>\$1,582,000</u>	<u>\$ 120,000</u>	<u>\$(589,000)</u>	<u>\$995,000</u>	<u>\$ 118,000</u>
Year ended December 31, 2000					
Allowance for uncollectible .....	<u>\$ 361,000</u>	<u>\$1,312,000</u>	<u>\$ 0</u>	<u>\$ 91,000</u>	<u>\$1,582,000</u>
Year ended December 31, 1999					
Allowance for uncollectible .....	<u>\$ 395,000</u>	<u>\$ 81,000</u>	<u>\$ 0</u>	<u>\$115,000</u>	<u>\$ 361,000</u>

(A) Impact of the deconsolidation of Spinnaker Industries, Inc. on September 30, 2001 (as discussed in Note 1 to the Consolidated Financial Statements included elsewhere herein).

(B) Uncollectible accounts written off are net of recoveries (majority attributable to Spinnaker in 2001).

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LYNCH CORPORATION

BY:                     /s/ RALPH R. PAPIITTO                      
   RALPH R. PAPIITTO  
   *Chief Executive Officer*  
   *(Principal Executive Officer)*

March 31, 2002

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Capacity</u>	<u>Date</u>
<u>          /s/ MARIO J. GABELLI                                    </u> MARIO J. GABELLI	Vice Chairman of the Board of Directors and Director	March 31, 2002
<u>          /s/ RALPH R. PAPIITTO                                    </u> RALPH R. PAPIITTO	Principal Executive Officer, Chairman of the Board of Directors and Director	March 31, 2002
<u>          /s/ E. VAL CERUTTI  </u> E. VAL CERUTTI	Director	March 31, 2002
<u>          /s/ AVRUM GRAY  </u> AVRUM GRAY	Director	March 31, 2002
<u>          /s/ RICHARD E. MCGRAIL                                    </u> RICHARD E. MCGRAIL	President, Chief Operating Officer and Director	March 31, 2002
<u>          /s/ RAYMOND H. KELLER                                    </u> RAYMOND H. KELLER	Principal Financial and Accounting Officer and Director	March 31, 2002

## EXHIBIT INDEX

<u>Exhibit No.</u>	<u>Description</u>
2 (a)	Asset Purchase Agreement (“Asset Purchase Agreement”) dated January 18, 2002 by and among Spinnaker Industries, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and SP Acquisition, LLC.††
(b)	Asset Purchase Agreement Amendment No. 1 dated February 15, 2002.††
(c)	Asset Purchase Agreement Amendment No. 2 dated February 25, 2002.††
(d)	Asset Purchase Agreement Amendment No. 3 dated March 5, 2002.††
(e)	Asset Purchase Agreement Amendment No. 4 dated March 8, 2002.††
(f)	Asset Purchase Agreement Amendment No. 5 dated March 18, 2002.††
(g)	Schedules to Asset Purchase Agreement dated January 18, 2002.††
(h)	United States Bankruptcy Court Order dated March 6, 2002; In Re: Spinnaker Industries, Inc., et al., C.A. No. 01-38066.††
3 (a)	Restated Articles of Incorporation of Registrant (incorporated by reference to Exhibit 3(a) of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 1987).
(b)	By-laws of the Registrant, (incorporated by reference to the Exhibit 3(b) of the Registrant’s Annual Report on Form 10-K for the year ended December 31, 1987).
4 (a)	Purchase Agreement, dated October 18, 1996 (the “Purchase Agreement”) among Spinnaker Industries, Inc., a Delaware corporation (“Spinnaker”), Brown-Bridge Industries, Inc., a Delaware corporation (“Brown-Bridge”), Central Products Company, a Delaware corporation (“Central Products”), and Entoleter, Inc., (“Entoleter”) and together with Brown-Bridge and Central Products, (the “Guarantors”) and BT Securities Corporation (the “Initial Purchaser”) (incorporated by reference to Exhibit 4.1 to Registrant’s Form 8-K, dated October 23, 1996).
(b)	Indenture, dated October 23, 1996, among Spinnaker, the Guarantors and the Chase Manhattan Bank, as Trustee (incorporated by reference to Exhibit 4.3 to Registrant’s Form 8-K, dated April 19, 1996).
(b) (i)	First Supplemental Indenture dated as of March 17, 1998, among Spinnaker Industries, Inc., Central Products Company, Entoleter, Inc., Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and the Chase Manhattan Bank, as Trustee (incorporated by reference by Exhibit 99.6 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998.)
(c)	Credit Agreement (the “Spinnaker Credit Agreement”) amended as of December 31, 1997, among Central Products Company, Brown-Bridge Industries, Inc. and Entoleter, Inc. as Borrowers, Spinnaker Industries, Inc. as Guarantor, each of the financial institutions listed on Schedule 1 thereto, BT Commercial Corporation, as Agent, Transamerican Business Credit Corporation, as Collateral Agent, and Bankers Trust Company as Issuing Bank (incorporated by reference to Exhibit 99.1 to Registrant’s Form 8-K dated October 23, 1996).
(c) (i)	Fourth Amendment to the Spinnaker Credit Agreement (incorporated by reference to Exhibit 9.3 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
(c) (ii)	Fifth Amendment to Spinnaker Credit Agreement (incorporated by reference to Exhibit 9.4 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
(c) (iii)	Sixth Amendment to the Spinnaker Credit Agreement (incorporated by reference by Exhibit 9.5 to the Form 8-K of Spinnaker Industries, Inc. dated as of March 17, 1998).
(d)	Refinanced Credit Agreement among Spinnaker Coating, Inc., Spinnaker Coating-Maine, Inc. and Entoleter, Inc. as Borrowers, Spinnaker Industries, Inc. as Guarantor, each of the financial institutions listed as Schedule 1 hereto and Transamerica Business Corporation, as Agent, dated August 9, 1999 and the First, Second and Third Amendments thereto (incorporated by reference to Exhibits 10.5, 10.6, 10.7 and 10.8 to Spinnaker’s Form 10-K for the year ended December 31, 1999).

<u>Exhibit No.</u>	<u>Description</u>
(d) (i)	Fourth Amendment to financed Credit Agreement dated April 17, 2000 (incorporated by reference to Exhibit 10.1 to Spinnaker's Form 10-Q for the quarter ended March 31, 2000).
(d) (ii)	Fifth Amendment to Refinanced Credit Agreement dated September 30, 2000 (incorporated by reference to Exhibit 10.1 to Spinnaker's Form 10-Q for the quarter ended September 30, 2000).
(d) (iv)	Sixth Amendment to Refinanced Credit Agreement dated March 2001 (incorporated by reference to Exhibit 10.16 to Spinnaker's Form 10-K for the year ended December 31, 2001).

The Registrant, by signing this Form 10-K Annual Report, agrees to furnish to the Securities and Exchange Commission a copy of any long-term debt instrument where the amount of the securities authorized thereunder does not exceed 10 percent of the total assets of the Registrant on a consolidated basis.

- 10 (a) \* Lynch Corporation 401(k) Savings Plan.
- (b) Acquisition Agreement between Brown-Bridge Acquisition Corporation and Kimberly-Clark Corporation, dated June 15, 1994 (exhibit omitted) (incorporated by reference to Exhibit 10<sup>®</sup> to Registrant's Form 10-Q for the quarter ended June 10, 1994).†
- (c) \* Management Agreement, dated as of June 10, 1994, by and among Boyle, Fleming, George & Co., Inc. and Safety Railway Service Corporation (incorporated by reference by Exhibit 7.1 to the Registrant's Form 8-K, dated June 13, 1994).
- (d) Subscription Agreement dated March 9, 2000 between Registrant and Mario J. Gabelli (incorporated by reference to Exhibit E to Amendment No. 41 to Schedule 13D of Registrant dated March 15, 2000 filed by Mario J. Gabelli et. al.).
- (e) Warrant Purchase Agreement dated as of June 10, 1994, by and among Boyle, Fleming, George & Co., Inc. and Safety Railway Service Corporation (incorporated by reference by Exhibit 7.1 to the Registrant's Form 8-K, dated June 13, 1994).
- (f) A Warrant, dated as of June 10, 1994, executed by Safety Railway Service Corporation (incorporated by reference to Exhibit 7.1 to Registrant's Form 8-K, dated June 12, 1994).
- (g) Asset Purchase Agreement, dated as of June 15, 1994, between Kimberly-Clark Corporation and Brown-Bridge Acquisition Corp. (Exhibits omitted) (incorporated by reference to Exhibit 10<sup>®</sup> to Registrant's Form 10-Q for the quarter ended June 30, 1994).†
- (h) Stock Purchase and Loan Program (incorporated by reference to Exhibit 10(p) to Registrant's Form 10-K for the year ended December 31, 1994).
- (i) Shareholders' and Voting Agreement, dated September 16, 1994, among Safety Railway Service Corporation, Brown-Bridge Industries, Inc. and the other stockholders of Brown-Bridge (incorporated by reference to Exhibit 10(q) to Registrant's Form 10-K for the year ended December 31, 1994).
- (j) Put Option Agreement, dated September 16, 1994, among Safety Railway Service Corporation, Brown-Bridge Industries, Inc. and certain stockholders of Brown-Bridge (incorporated by reference to Exhibit 10(q) to Registrant's Form 10-K for the year ended December 31, 1994).
- (k) \* Directors Stock Plan (incorporated by reference to Exhibit 10(o) to Registrant's Form 10-K for the year ended December 31, 1997).
- (l) Amended Phantom Stock Plan (incorporated by reference to Exhibit 10(p) to Registrant's Form 10-Q for the year ended September 30, 1998).
- (m) Stock and Asset Purchase Agreement, dated as of September 27, 1995, by and among Central Products Acquisition Corp. Unisource Worldwide, Inc. and Alco Standard Corporation (incorporated by reference to Exhibit 7.1 to Registrant's Form 8-K, dated October 19, 1995).†
- (n) Agreement and Plan of Merger (Brown-Bridge Minority Interest), by and among Spinnaker Industries, Inc., BB Merger Corp., Brown-Bridge Industries, Inc. and the stockholder of Brown-Bridge Industries, Inc. on Exhibit A thereto (incorporated by reference to Exhibit 99.2 to Registrant's Form 8-K, dated April 19, 1996).†
- (o) Lease Agreement between Registrant and Gabelli Funds, Inc. (incorporated by reference to Exhibit 10(a)(a) to Registrant's Form 10-Q for the Quarter Ended March 31, 1998).

<u>Exhibit No.</u>	<u>Description</u>
(p)	Asset Purchase Agreement, dated as of November 18, 1997, by and between S.D. Warren Company (“Seller”) and Spinnaker Industries, Inc. (incorporated by reference to Exhibit 2.1 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).
(p) (i)	First Amendment to Asset Purchase Agreement, dated March 17, 1998, by and between S. D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 4.2 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).†
(p) (ii)	Subordinated Note, dated March 17, 1998, issued by Spinnaker Industries, Inc. to S.D. Warren Company in the original principal amount of \$7 million bearing interest at a rate of 20% per annum (incorporated by reference to Exhibit 4.1 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998).
(p) (iii)	Site Separation and Service Agreement, dated March 17, 1998, between S.D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 99.1 to the Form 8-K of Spinnaker Industries, Inc., dated March 17, 1998).
(p) (iv)	Lease Agreement, dated March 17, 1998, between S.D. Warren Company and Spinnaker Industries, Inc. (incorporated by reference by Exhibit 99.2 to the Form 8-K of Spinnaker Industries, Inc., dated as of March 17, 1998.)
(q)	Stock Purchase Agreement between Spinnaker Industries, Inc. and Intertape Polymer Group, Inc., dated April 9, 2000 (incorporated by reference to Exhibit 2.1 to Spinnaker Industries, Inc. Form 8-K, dated August 16, 2000).
(r)	Asset Purchase Agreement by and among Registrant, Spinnaker Electrical Tape Company and Intertape Polymer Group, Inc., dated April 9, 2000 (incorporated by reference to Exhibit 2.2 to Spinnaker Industries, Inc. Form 8-K, dated August 16, 2000).
(s)	Information Statement of Lynch Interactive Corporation’s (incorporated by reference to Exhibit 99.1 to Lynch Interactive Corporation’s Form 10-A-1, dated August 18, 2000).
(t)	Separation Agreement, dated as of August 31, 2000, between Registrant and Lynch Interactive Corporation (incorporated by reference to Exhibit 2 to Lynch Interactive Corporation’s Form 10a-1, dated August 18, 2000).
(u) *	Letter of Understanding between Registrant and Louis A. Guzzetti (incorporated by reference to Exhibit (u) to Registrant’s Form 10-K for the year ended December 31, 1999).
(v)	Note from Louis A. Guzzetti, Jr. to Registrant (incorporated by reference to Exhibit 10(v) to Registrant’s Form 10-K for the year ended December 31, 2000).
(w) *	Agreement among Registrant, Mario J. Gabelli and Ralph R. Papitto dated August 17, 2001 pursuant to which, among other things, Registrant agreed to grant Mr. Papitto an option (incorporated by reference to Exhibit 10(w) to Registrant’s Form 8-K dated August 17, 2001).
(x) *	Amendment dated February 7, 2002 among Registrant, Mario J. Gabelli and Ralph R. Papitto, amending the Agreement at Exhibit 10(w) to terminate Registrant’s obligation to grant an option to Mr. Papitto.††
(y) *	Lynch Corporation 2001 Equity Incentive Plan adopted December 10, 2001.††
16	Letter Re: Change in Certifying Accountant (incorporated by reference to Exhibit 16 to Registrant’s Form 8-K, dated March 19, 1996).
21	Subsidiaries of the Registrant.††
23	Consent of Ernst & Young LLP.††
24	Powers of Attorney.††

\* Management contract or compensatory arrangement.

† Registrant agrees to furnish a supplemental copy of any omitted schedule to the Securities and Exchange Commission upon request.

†† Filed herewith.

The Exhibits listed above have been filed separately with the Securities and Exchange Commission in conjunction with this Annual Report on Form 10-K or have been incorporated by reference into this Annual Report on Form 10-K. Lynch Corporation will furnish to each of its shareholders a copy of any such Exhibit for a fee equal to Lynch Corporation's cost in furnishing such Exhibit. Requests should be addressed to the Office of the Secretary, Lynch Corporation, 50 Kennedy Plaza, Suite 1250, Providence, RI 02903.